S. HRG. 99-28

THE VA HOME LOAN GUARANTY PROGRAM AND H.R. 2801

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND MEMORIAL AFFAIRS

OF THE

COMMITTEE ON VETERANS' AFFAIRS
HOUSE OF REPRESENTATIVES

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THE VA HOME LOAN GUARANTY PROGRAM AND H.R. 2801

THURSDAY, SEPTEMBER 12, 1985

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS,
COMMITTEE ON VETERANS' AFFAIRS,
Washington, D. C.

The subcommittee met, pursuant to notice, at 9:05 a.m., in room 335 Cannon House Office Building, Hon. Richard C. Shelby (chairman of the subcommittee) presiding.

Present: Representatives Shelby, Mollohan, Bryant, Sundquist, and Rowland of Connecticut

OPENING STATEMENT OF CHARIMAN SHELBY

Mr. SHELBY. The subcommittee will be in order.

This morning we meet to hold an oversight hearing on the VA Home Loan Guaranty Program. Our previous hearings this year disclosed the VA loan guaranty revolving fund was experiencing severe financial difficulties due to the high default and foreclosure rates. Appropriations were necessary in both fiscal years 1984 and 1985 to keep the program solvent.

Earlier this year the Administration proposed to increase the VA guaranteed home loan origination fees from 1 percent to 5 percent for revenue purposes. The committee firmly believed that this "quick fix" solution was not the answer. Rather, this would have resulted in a back door approach to killing the program, not helping it. Fortunately, the Congress rejected this proposal. Nevertheless, the future financing of the program remains a major concern.

At our last hearing, VA officials stated that they were carrying an inventory of approximately 22,000 properties estimated at a value of $800 million and were still acquiring over 2,000 properties monthly. Members of the subcommittee expressed major concern about the size of the inventory, and we will be hearing from the VA on their recent efforts to sell these homes.

Recent news articles have reported on several manufactured housing industry invoicing practices and on the VA Inspector General's ongoing investigation. The subcommittee is very concerned about these reports, and I am pleased that we will be hearing from the Assistant Inspector General as well as officials from the manufactured housing industry.

Hopefully, as a result of this hearing, we can get everybody back on the right track.

Lastly, today the subcommittee will consider the provisions of H.R. 2801, a bill introduced by Congressman Sundquist of Tennessee in response to his concern over the VA's high property inventory. This bill would establish a discounted sales program on foreclosed properties for veterans.

Our first witness this morning is Mr. Raymond J. Vogel, Chief Benefits Director of the Veterans' Administration.

Mr. Vogel, please come on up. Your complete written testimony will be made a part of the record, without objection. I would appreciate it if you would briefly sum up your remarks so that we will have enough time to question you.

STATEMENT OF RAYMOND J. VOGEL, CHIEF BENEFITS DIRECTOR, VETERANS' ADMINISTRATION; ACCOMPANIED BY ROBERT M. O'TOOLE, DIRECTOR, LOAN GUARANTY SERVICE; AND JAMES P. KANE, ASSISTANT GENERAL COUNSEL

Mr. VOGEL. Yes, sir. Thank you, sir.

Mr. Chairman and members of the subcommittee, it is a pleasure to appear before you this morning to discuss the operation of the Veterans' Administration's housing program. I have with me today Robert M. O'Toole, Loan Guaranty Service Director, and James P. Kane, Assistant General Counsel of the Veterans' Administration.

Mr. Chairman, your invitation to appear before the subcommittee requested we discuss a number of specific areas, including the future financing of the loan guaranty program. In recent years the loan guaranty revolving fund has been substantially depleted. Appropriations of over $560 million were needed in fiscal years 1984 and 1985 in order to enable the program to meet its obligations. Current budget projections indicate an end-of-year unobligated balance of approximately $230 million, therefore requiring no supplemental appropriation for the remainder of fiscal year 1985.

We are currently making every effort to maximize sales, both cash sales of properties and vendee loan sales, and thus reduce appropriations. This fiscal year to date we have received $254 million in cash proceeds from the sale of properties and $681 million from the sale of vendee loans. While the revolving fund is still facing financial difficulties, we are hopeful that a continued reduction in our inventory of acquired properties will lessen future funding requirements.

Mr. Chairman, you also requested that we discuss current property management practices. Although we continue to experience high levels of foreclosures, we have made considerable progress in our property sales volume and expect this trend to continue. Property sales through July are 22 percent higher than the comparable period last year. We expect that fiscal year 1985 property sales will exceed 28,000 and will generate $1.2 billion in revenue to the loan guaranty revolving fund.

We have reduced our property inventory by 16 percent during fiscal year 1985 and implemented two provisions of the Deficit Reduction Act of 1984: Collection of a 1 percent funding fee for sales completed with vendee financing and sale of a minimum of 25 percent of VA properties for cash. Through July, we have collected over $97 million in funding fees required by the act, $7 million of

which was collected for vendee loans; 26.7 percent of our sales this year have been for cash. Through July, we had 18,783 properties in inventory, down from our record high of 22,316 in March 1984.

Several successful program changes have been implemented to promote sales which include considering below-list offers on properties that have been on the market for more than 6 months, sales commission bonuses of up to $500 on hard-to-sell properties, allowing a 10 percent discount for those purchasers who can pay cash, paying reasonable discount points for outside financing if obtained by the purchaser, and using real estate auctions to sell properties in areas where sales efforts have been unsuccessful.

We have held auctions in Detroit, Houston, Peoria, and Cedar Rapids, selling 696 properties for over $11.5 million. Future auctions are scheduled for Portland, Phoenix, and Los Angeles.

Mr. Chairman, another item you wished to discuss was H.R. 2801, which would authorize the Administrator to sell at a discount properties acquired by VA to certain veterans. Under H.R. 2801, if VA has been unable to sell a property for at least 3 months, it would be sold at a discount to a veteran who has never previously owned a home and who has VA home loan entitlement. The discount could be up to 30 percent depending on how long the property has been in the VA's inventory.

Once VA acquires a property, we undertake to sell it in order to recoup at least a portion of our loss on a guaranty. Our primary goal in selling these properties is to receive the best possible price and terms in order to maximize the Government's sale price for acquired properties, and that any discount deemed desirable to dispose of the properties should be available to any qualified buyer.

VA estimates that enactment of H.R. 2801 would result in a net reduction of sales volume of approximately $115 million in fiscal 1986 and a 5-year net reduction of $474.5 million. Accordingly, Mr. Chairman, while VA opposes enactment of H.R. 2801 as not being timely, we will keep it under consideration should our other attempts to sell properties not prove fruitful.

A final item requested for discussion was the recent frauds perpetrated by the manufactured housing industry and the actions the Veterans' Administration will take in response. The specifics of the manufactured home invoice padding scheme are covered in the testimony of the VA Inspector General's office.

In the early stages of the investigation, at the request of the Office of the Inspector General it was agreed that no changes in procedures would be made. We are now, after consultation with the Inspector General, considering changes in procedure to assure that such fraudulent practices will not occur in the future. One proposal under consideration is to revise the current dealer invoice certification to require full disclosure of all rebates or discounts received by the manufactured home dealer from the manufacturer, including volume purchase discounts.

Mr. Chairman, I am sure the committee would also be interested in knowing current actions in the area of underwriting. VA will continue to strive to ensure that only financially capable, creditworthy veterans receive VA home loans. Realizing the effects of continued high levels of defaults and foreclosures coupled with the disinflation in home prices, we issued a policy statement in May of

this year to all VA regional offices. The statement re-emphasized the importance of quality underwriting with particular attention devoted to avoiding the following unacceptable practices:

—Accepting at face value, without details and documentation, a borrower's explanation for a bad credit history.

—Approving loans based on an emotional appeal from the borrower, sales agent, or seller.

—Reopening and reversing a previous decision to reject a loan without new and compelling information.

—Approving marginal applications without adequate review and discussion among a group of underwriters where possible.

—Failing to require a borrower who is weak in one area, such as cash assets, to demonstrate strength in other areas, such as income and credit history.

—Unjustifiable reliance upon short-term or irregular income to qualify a borrower for a loan.

Our offices were also instructed to review and update the figures used to estimate family support requirements and maintenance and utility expenses. These figures are now made available to interested lenders. We are also developing a computerized capability to better identify lenders with a higher than acceptable record of defaulted loans.

Mr. Chairman, this concludes my statement. I will be pleased to respond to any questions that you or members of the subcommittee may have.

[The statement of Raymond J. Vogel appears at p. 53.]

Mr. SHELBY. I have several questions. However I would like to first get into the housing inventory that has concerned a lot of us. I have been around the country and held some hearings and I have been to some regional offices where I have actually been in the field and looked at a number of houses, or inventory, or whatever you want to call them. I know this is a continuing problem when you are taking in a couple of thousand a month.

Is that about right, Mr. O'Toole?

Mr. O'TOOLE. Yes, sir.

Mr. SHELBY. I know you have reduced it according to the information I have. However the gentleman from Tennessee and I are both interested in ways to help the VA dispose of all properties. It has been my personal experience that the longer a piece of property remains vacant, something happens to it, and it deteriorates. Sooner or later, you and HUD, will take a loss on this.

Ultimately, aren't we all interested in moving properties as best we can? I know that with your discretionary authority you have tried some pilot programs to see how they work, from auctions on down. But it seems your property inventory is a chronic problem. At times it appears to be getting better, then it regresses.

What can we in the Congress do to help you move this inventory? Sooner or later the market forces work, and realtors will sell the properties. You are not going to get any more for them than actually what somebody would pay sooner or later.

Mr. VOGEL. Yes, sir.

Mr. SHELBY. Just carrying them on your books is really not helping anything. I think you are probably taking some licks.

Mr. VOGEL. Yes, sir.

Mr. SHELBY. I would be interested in your comments. I know the gentleman from Tennessee would be, too.

Mr. VOGEL. We are more than a little encouraged by the results in the last few months where our sales have exceeded our acquisitions. Coupled with that, we are also very concerned about the continued high level of defaults.

Mr. O'Toole just concluded conferences with his loan guaranty officers throughout the country and there is more than a little concern about the level of default there. But we are, in fact, selling more that we are acquiring and the inventory is down—while it is still a rather alarming figure, it gives us some measure of optimism.

Mr. SHELBY. Mr. Vogel, let me jump in for a second. In your underwriting, and I know that under the VA guaranty program it was mandated by Congress that it would be, for lack of a better word, lenient, in trying to provide housing for veterans who might not qualify for conventional financing. That was why Congress enacted the law to begin with and kept it going.

Could you tighten up on some of the underwriting requirements without really stifling the program?

Mr. VOGEL. Yes, sir.

Mr. SHELBY. In other words, for a veteran to meet the eligibility requirement to get a VA home loan, they still have to be employed or must have income to meet those payments on a house. Right?

Mr. VOGEL. Yes, sir.

Mr. SHELBY. If you tighten up underwriting criteria, what would that do to the foreclosure rate?

Mr. VOGEL. We are looking very closely at our underwriting. We think basically that our underwriting is sound. We are certainly not doing a veteran any favor by being overly lenient in granting him a loan to buy a house that he can't afford to retain.

We have looked at the Mortgage Bankers Association's study of the program and the work done by the VA's Inspector General on tightening up the underwriting.

Mr. SHELBY. Doesn't everybody lose in a sense if you approve a questionable loan for a veteran which he can't really afford and which subquently goes to foreclosure? The mortgage banker certainly isn't any better off. If something is put on the books, the banks try to collect it. They will take a loss in a sense, won't they?

Mr. VOGEL. Yes, sir.

Mr. SHELBY. You will take a loss and so will the taxpayer. The veterans are no better off to have lost their home and conquently owe a debt to the Government.

Mr. VOGEL. No, sir.

Mr. SHELBY. It therefore looks to me like some of it could start there. I am not saying it is the whole answer.

Mr. VOGEL. I quite agree with you, sir.

Mr. SHELBY. Is there any way other than the ideas you have mentioned to move your inventory?

Mr. VOGEL. Other than those that I have referred to in the testimony. I think that pretty well covered the kinds of marketing efforts we are making.

If Mr. O'Toole would like to address that I would be pleased to turn to him.

Mr. O'TOOLE. Mr. Chairman, I think we have many of the things that we need. Certainly the fact that through the Deficit Reduction Act last year we were able to retain the ability to provide vendee financing on those houses that we sell. We have worked very closely with a task force from the NAR—the National Association of Realtors—on what we can do in certain areas to get the word out to the community of real estate people, real estate professionals, that we have properties for sale and how we can move those.

I think all of those efforts are working in that our sales are over 25 percent above what they were last year.

Mr. SHELBY. Isn't a lot of that attributed to the economy? In other words, interest rates are lower and real estate prices have stabilized?

Mr. O'TOOLE. Well, that certainly helped. In some of the areas it has helped. But what we have done, we have moved some of the hard-to-sell houses.

Mr. SHELBY. Is there any way to enhance the marketing of these properties through the realtors or somebody?

Mr. O'TOOLE. Well, we haven't received the final report from the task force that the realtors put together. We will see if that is one of the things that they recommend.

Mr. SHELBY. I want to get into something you mentioned briefly, and that is the manufactured housing problem. What is the difference between volume rebates and discounts? In other words, what are permissible charges and what are not? And do you have any intention of formally issuing new, clarifying regulations as pertains to the manufactured housing industry?

Mr. O'TOOLE. We issued a circular in 1979 that attempted to define what a volume rebate is, and that policy statement said that if a company had a policy of offering to all the dealers that they were doing business with on an equal basis a rebate based on volume of business that would be acceptable to us. But certainly a rebate on individual units or a small volume purchase would not be eligible to be included in the invoice price in the certification.

The whole issue of what is an acceptable purchase price and what we base our loan amount on is something that is of concern to us. And once the IG began looking into this matter, of course, with our assistance, we realized that we were going to have to do something. We wanted to look at the whole issue, and we agreed that we would wait until a little more information was obtained by the IG to determine what should be done.

I don't know what we should do, but we obviously have to do something about it.

Mr. SHELBY. Mr. O'Toole, I know that the VA Manufactured Housing Program is different in some regards from a home that is conventionally built. As I understand it, you have qualified appraisers who go out and appraise, say, a house in Arlington, VA, based on their experience and their knowledge of property values.

Now what is the criteria that you use to put a value on a manufactured home? It has to be different, doesn't it?

Mr. O'TOOLE. Well, it is different.

Mr. SHELBY. Okay. That is what I am getting at.

Mr. O'TOOLE. The industry practice is different and it is based on the manufacturer's invoice plus 20 percent. I think we accepted that kind of a practice when we first became involved in the manufactured housing business because that is what industry practice was.

One of the things I think we are going to look at very closely is whether to move off that kind of a pricing system and move into something similar to what you mention, some kind of a fee appraisal system. The problem being we don't know if that is an acceptable practice in the industry, but we know that it is difficult to get fee appraisers who do that kind of work in manufactured housing.

Mr. SHELBY. They would need to have experience in that field.

Mr. O'TOOLE. That is right.

Mr. SHELBY. What we are interested in is how to rectify a problem and make the program work, isn't it?

Mr. O'TOOLE. Yes, Mr. Chairman.

Mr. SHELBY. Obviously, there is a problem there. I don't know that much about the automobile and truck business; however a manufacturer's price is certifed to an auto dealer. Isn't this a similar situation to manufactured housing dealing with big volume? Don't automobile dealers get a rebate or a discount, off of the list price from manufactures when they sell a substaintial number of their cars?

Is that where volume discounts for manufactured homes came from? In other words, just everyday business?

Mr. O'TOOLE. I think that is right. The normal practice the way I understood it was at the end of a year, if you did a lot of business with a certain mobile home dealer, then based on the volume there was a certain amount of a contribution made back to the dealer.

But the problem came in when they were doing it on an individual basis with a small volume. That almost every transaction had some sort of an amount, a contribution back to the dealer.

Mr. SHELBY. Rather than the aggregate?

Mr. O'TOOLE. That is right.

Mr. SHELBY. Say you did $5 million worth of business with us and I was X company manufacturing mobile homes. If such discounts were in the aggregate, would that have been permissible?

Mr. O'TOOLE. That is right. We wouldn't have had any problem with that.

Mr. SHELBY. But by breaking it down into individual units, then you say you can't do this as that violates VA regulations?

Mr. O'TOOLE. That is right.

Mr. SHELBY. Okay.

Mr. O'TOOLE. And it didn't have anything to do with the amount of the volume. You got that rebate no matter how many units you purchased from that manufacturer.

Mr. SHELBY. I know we have the Inspector General and the Assistant Deputy Inspector General coming in on another panel, so we will get into that further.

I believe the gentleman from Tennessee has some questions.

Mr. SUNDQUIST. Thank you, Mr. Chairman.

Thank you for your testimony, Mr. Vogel.

On the first page of your testimony you describe supplemental appropriations—$100 million, $160 million, $306 million.

Why was that needed?

Mr. VOGEL. It was needed because the amount needed from the revolving fund exceeded the amount in that fund, and the appropriations were needed to make it whole because of the——

Mr. SUNDQUIST. Why did that occur in the revolving fund?

Mr. VOGEL. Because of the large number of properties being carried in inventory and those after foreclosure, and the cost of carrying that property.

Mr. SUNDQUIST. The cost of carrying the property?

Mr. VOGEL. Yes, sir.

Mr. SUNDQUIST. Any cost of losses on property in that number?

Mr. VOGEL. Yes, sir.

Mr. SUNDQUIST. Interest?

Mr. VOGEL. Yes, sir.

Mr. SUNDQUIST. On page 2, you say "continued high level of defaults and foreclosures" and you talk about a continued reduction in inventory.

What is your projection? You now have 18,783 in inventory. What is your projection for the rest of this year and the next few months of next year in terms of where that inventory is going? Obviously you must be planning for this.

Mr. VOGEL. Yes, sir. We project the carried inventory of about 16,600 in 1986 and then it will drop down to about 14,200 in 1987, 12,700 in 1988, and so forth, down to in 1990 something a little less than 12,000 in inventory.

Mr. SUNDQUIST. So what is going to happen now when Houston hits shortly, with the problems? And there must be other areas of the country. You are going to have all the problems of Houston and other areas of the country and you are still going to drop this inventory down 3 or 4 months from now to less than what it is now. Is that correct?

Mr. VOGEL. The expectation is that while it may deepen in Houston it will be improving in other areas that were badly hit in the early 1980's that seem to be coming back, the upper Midwest.

Mr. SUNDQUIST. I hope you are right. I just wanted to have it for the record, so we can look back maybe early next spring and see how accurate that projection was.

You say the revolving fund is still facing financial difficulties?

Mr. VOGEL. Yes, sir.

Mr. SUNDQUIST. Are you going to have to come back again?

Mr. VOGEL. I am sorry, sir?

Mr. SUNDQUIST. Are you going to have to come back for some more money?

Mr. VOGEL. We feel that the sales this coming year, as we close out this year, will be such that we have not projected a need for an appropriation in fiscal 1987. In 1986—about $200 million in fiscal 1986.

Mr. SUNDQUIST. $200 million more?

Mr. VOGEL. Yes, sir.

Mr. SUNDQUIST. The point I want to make with that is we are putting a lot of money into that fund. Correct? I mean, we are talking about millions—$300 million, $200 million, $180 million.

Mr. VOGEL. Yes, sir.

Mr. SUNDQUIST. I congratulate you on your auctions. On the houses you sold in auction do we have a net gain over what they were listed as valued by the VA, or a net loss counting all the costs?

Mr. VOGEL. There is a very small net gain. There were four different auctions with different yields.

Mr. O'TOOLE. It depended on where we were.

Mr. SUNDQUIST. I am talking about the total.

Mr. O'TOOLE. The total, we sold them for 95 percent of what we had them listed for for auction.

Mr. SUNDQUIST. Sold them for 95 percent?

Mr. O'TOOLE. That is right. In other words, that is from a high of 150 percent in the Detroit auction to others that have been somewhat below the price.

Mr. SUNDQUIST. That includes all costs?

Mr. O'TOOLE. Yes, all costs.

Mr. SUNDQUIST. Except for the loss of interest on those houses that had been setting on the market for some time?

Mr. O'TOOLE. That is right.

Mr. SUNDQUIST. How much are we talking about? For the 18,783 homes that are setting there, how much are we talking about in interest for all of them per year, in round numbers?

Mr. O'TOOLE. Well, the average, of the 18,000, the average list price is around $43,000 at the Treasury rate of 9 percent, if that is a number that you want to use.

Mr. SUNDQUIST. Tell me what that figures out to be per year.

Mr. O'TOOLE. I don't have that, Mr. Sundquist.

Mr. SUNDQUIST. Well, maybe Mr. Vogel can be working on that while I ask my next question.

It is a sizable amount of money per year, I assume, if we are putting out $306 million, $160 million and $100 million, and you are going to have to come back for another $200 million. It is a sizable number, I assume, and hopefully we will have it here momentarily.

I did notice, Mr. O'Toole, on page 5 of the testimony—Mr. Vogel, you can go ahead and compute that, or if you have an estimate—

Mr. VOGEL. I don't yet, sir.

Mr. SUNDQUIST. Okay. Let me make sure I get back to the right page here.

"The sale of acquired properties has never been intended as a benefit for veterans." But isn't in fact the housing program a benefit program?

Mr. O'TOOLE. That is right. The Home Loan Guaranty Program is a benefit program, that is right.

Mr. SUNDQUIST. Under current law you do have the authority to offer certain properties at discount. Depending on what the size of that number is, but just based on the fact that we have been talking about $100 million, $160 million, $306 million, and another $200 million, why aren't you discounting more if the net gain for you in terms of interest received is a plus over the inventory that is setting there losing interest and deteriorating in condition?

Mr. O'TOOLE. I think that is one of the reasons we sold so many houses; in certain instances we price houses to move them. But what we lose in interest income certainly is a lot smaller amount than we would by taking heavy discounts.

Mr. SUNDQUIST. What is heavy?

Mr. O'TOOLE. Well, more than 20 percent I would say.

Mr. SUNDQUIST. Mr. Vogel, if you want to do that later, I would be glad to wait. I was just curious, to know how much we are talking about.

Mr. VOGEL. Well, if you took the figures that I heard Mr. O'Toole say, as he read them through—18,000 properties at $43,000 a property at 9 percent simple interest—$6 million, almost $7 million to carry that interest.

Mr. SUNDQUIST. $7 million per year?

Mr. VOGEL. Yes, sir.

Is that right?

Mr. O'TOOLE. That sounds awful high.

Mr. SUNDQUIST. No, it doesn't sound high to me at all. We will leave that for a later discussion.

On page 6, you talk about the fact that veterans may delay their purchase offers in order to take advantage of a discount—excuse me, I am sorry, its the next paragraph—and this may invite fraud and abuse. I am told by counsel a simple amendment would handle that.

I would like to talk about your number for just a minute. I would like to have you explain to me the rationale of the $474.5 million net reduction and the $115 million in FY 1986 costs.

Mr. O'TOOLE. Okay.

Mr. SUNDQUIST. The first question is you based it on what percentage average?

Mr. O'TOOLE. Well, we based it on the number of properties that we have that fall into the categories in the proposal. And then after that—it is the worst case possible. The worst case being that everything that was eligible to be sold under the program would be sold with that discount.

Mr. SUNDQUIST. Is that based on 30 percent average? That is what I was told.

Mr. O'TOOLE. No.

Mr. SUNDQUIST. It is not? What discount percentage was that based on?

Mr. O'TOOLE. It was based on looking at the inventory that we have right now-

Mr. SUNDQUIST. What is the average?

Mr. O'TOOLE. For example, 15 percent of the inventory falls into the category we have owned between 3 and 7 months, 15 percent between 7 months and a year, and 30 percent we have had for over a year.

Mr. SUNDQUIST. 30 percent of the properties—

Mr. O'TOOLE. That is right.

Mr. SUNDQUIST [continuing]. That you have you have held for over a year?

Mr. O'TOOLE. That is right.

Mr. SUNDQUIST. 30 percent of all the 18,783 houses have been held for over a year?

Mr. O'TOOLE. That is right.

Mr. SUNDQUIST. Did that take into account lost interest, the $115 million?

Mr. O'TOOLE. We calculated the gain in interest in the $115 million. In other words, when we calculated what the cost of the discount would be we added in what the gain in the interest would be by having that money sooner.

Mr. SUNDQUIST. The fact that you had it back on the rolls for that same year, is that the way you computed it?

Mr. O'TOOLE. Well, we took into consideration the interest savings.

Mr. SUNDQUIST. Did you take into consideration what you were going to have to do to remodel that house when it has been setting for over a year?

Mr. O'TOOLE. We took the average loss, and the average holding time, but we didn't make any presumptions that we would include any kind of repair program.

Mr. SUNDQUIST. So you don't think you are going to have to repair a house after it has been setting there for a year?

Mr. O'TOOLE. Well, we don't repair a lot of them.

Mr. SUNDQUIST. That is not what I asked. I mean when you are precise in one figure and then say we don't repair a lot of them, that is not very precise, Mr. O'Toole, in all respect.

Secondly, there is some reason those houses that have been held over a year aren't selling. Right?

Mr. O'TOOLE. That is right.

Mr. SUNDQUIST. Is it possible that those houses might be overvalued?

Mr. O'TOOLE. It is possible.

Mr. SUNDQUIST. Can you, Mr. Vogel or Mr. O'Toole, tell me, of your entire inventory, how close is it to what you value it as?

Mr. O'TOOLE. I think one of the reasons that we have been able to move so many houses in the last year is because we have told our officers they have to be a lot more—the prices have to be more consistent with what the markets are in their communities.

Mr. SUNDQUIST. I had asked the realtors to look at some of those houses in Shelby County, in Memphis.

Mr. O'TOOLE. Yes.

Mr. SUNDQUIST. Let me tell you a lot of them are way overvalued. What I am asking is, are you afraid to have a real valuation of what those properties are worth because in fact this fund may be in worse shape than we think it is?

Mr. O'TOOLE. If you are asking if we are afraid of somebody telling us what those properties are worth, no, we are not.

Mr. SUNDQUIST. There has got to be a reason the property hasn't sold and 30 percent of your properties have been held over a year. Based on that it tells me that the current property you are taking in you are able to move, but your old property you are not.

Mr. O'TOOLE. Well, we have had a problem moving some of the older properties. That is why we have reduced some of the ones we have had in inventory for over two years to a very small number. When we first started looking at this inventory—

Mr. SUNDQUIST. Let me yield to my chairman.

Mr. SHELBY. I thank the gentleman from Tennessee for yielding.

Some of those thoughts ran through my head, too, regarding the inventory you are carrying. It reminds me of some people having some old long term bonds in a portfolio which will not yield as

much due to today's higher interest rate fluctuations. Could that possibly be true of some of the properties you are carrying? Could you furnish us a breakdown on your properties as well as their age and location?

We are interested in the truth of the real condition of the Loan Guaranty Revolving Fund and the inventory.

Mr. O'TOOLE. We will be happy to provide that information for the record.

[The referred to information appears on p. 61.]

Mr. SHELBY. I thank the gentleman for yielding.

Mr. SUNDQUIST. I thank my chairman.

What I have been trying to propose, and nothing is set in concrete, is if I were in business and had a big inventory and was going broke and had to go to somebody for some more money, I would want to turn over the inventory somehow. I would rather go to a veteran who has never been able to buy a home before, and if I had a home that was there for $30,000 and could sell it to that veteran for $24,000 or $21,000 or $22,000 and not put any money into it and not have to hold it in inventory and have the loss of interest, I would rather have it back in his or her hands and lower what I have, even if it means facing up to the fact that what I have got in inventory may not be worth what I am holding it as. That was the whole concept. That was the question.

With respect to your estimate of $115 million, how is it that CBO says it is $60 million?

Mr. O'TOOLE. Mr. Sundquist, I haven't seen the CBO estimate. As I said, the $115 million is based on the fact that every property that falls into the category in the bill would be sold with that discount. I haven't seen the CBO estimate.

Mr. SUNDQUIST. Well, we have to go by CBO for legislative purposes when it comes to costs, and to have the difference between $60 million and $115 million seems to me to be a fairly big figure.

Mr. O'TOOLE. We would be happy to share our cost estimate with CBO, and we would be happy to look at the CBO estimate.

Mr. SUNDQUIST. Do you have any estimate on how much interest we are talking about with the 18,000 properties? Did you compute that?

Mr. O'TOOLE. I think we are going to have to provide that.

[Subsequently the Veterans Administration provided the following information for the record:

With 18,000 properties in inventory at an average list price of $43,000 and the Treasury rate of 9 percent, the annual interest for these properties amounts to approximately $70 million.]

Mr. SHELBY. The gentleman's time has expired.

Mr. SUNDQUIST. Thank you.

Mr. SHELBY. The Chair recognizes the gentleman from Connecticut, Mr. Rowland.

Mr. ROWLAND. Thank you, Mr. Chairman. First let me thank you and my colleague from Tennessee for your interest in this issue and the public hearing today.

Mr. Vogel, I just have a couple of questions. With regard to the manufactured home industry, they are obviously concerned about their image and the fact that it may be tarnished by those who vio-

lated the law. In your testimony you say you are considering some changes, and I think in the testimony you mentioned one.

Any other thoughts or comments you would care to make on that?

Mr. VOGEL. Beyond those offered, sir, no, sir.

Mr. ROWLAND. So the only real consideration has been the one offered in your testimony?

Mr. O'TOOLE. Well, Mr. Rowland, we certainly feel that we have got to look at the item we talked about before, how we determine what the loan amount is, and that is the issue that is of concern. We don't know what to do about that, but we are concerned about it enough so that we are going to do something about it.

Mr. ROWLAND. It has been suggested by some that the VA appraise the manufactured homes as is customarily done with others. How do you feel about that?

Mr. O'TOOLE. Well, that is an area that we are going to take a look at. The problem with that appears to be that that is not the way the industry works, and we would have a situation where the VA program, which is a small percentage of all the units that are sold, would have a separate way of determining purchase price and loan amount. If that is what we have to do to clean it up, then, unfortunately, that is what we will have to do.

Mr. ROWLAND. In recognizing VA's efforts to curb any fraud or abuse in this program, what is your overall assessment of the program?

Mr. O'TOOLE. Well, I think I would rather withhold that assessment until the Office of the Inspector General completes all of their work to see how many other firms are going to be involved in the scheme.

Mr. ROWLAND. Okay. Thank you. Thank you, Mr. Chairman.

Mr. SUNDQUIST. Would the gentleman yield?

Mr. ROWLAND. Be glad to.

Mr. SUNDQUIST. Our computations up here indicated $70 million per year and not $6 million. But if you would furnish that for the record, I would appreciate it.

Mr. SHELBY. The Chair recognizes the gentleman from Texas, Mr. Bryant.

Mr. BRYANT. Thank you, Mr. Chairman.

Mr. Vogel, I won't press on the issue of manufactured housing if the experts are yet to come. I don't know which of you is making the policy in this area.

But I think there is possibly a problem in dealing with the manufactured housing industry here if the regulations that relate to what their invoices are supposed to reflect are somehow obscure in any way. You seemed to indicate that maybe that was the case, particularly in terms of defining what a volume discount is, what's the difference in a volume discount and a small discount. I didn't hear it if you did it already, but would you define what a volume discount is, or tell me what the regulations say?

Mr. VOGEL. We define a volume rebate, as stated in our DVB circular 26-79-34, as an established company marketing practice offered to all dealers on an equal basis for volume purchases over a stated period of time. Rebates on single units or small volume pur-

chases are not considered eligible to be included in the invoice price with a loan amount for VA purposes.

Mr. BRYANT. How do small volume purchases differ from volume purchases? How do you define a small volume purchase in the regulations?

Mr. VOGEL. I don't think that that is in fact defined in the regulations, sir. No, sir, it is not.

Mr. BRYANT. Well, if the regulation then says that you are going to allow volume discounts to apply but not small volume discounts, how does one accurately read the regulation, if you don't define small volume discounts?

Mr. KANE. As I understand it, when the program began back in the 1970's this question did come up, and those who had concern with the question of what would be an acceptable practice and what would not were in touch with us, and we did try to look at it, I think, on a case-by-case basis. It depends on the size of the manufacturer. What is small for a manufacturer who makes 250 units a year might be nothing for a manufacturer who makes 10,000 units. The manufacturers in this industry evidently vary greatly in size of the volume that they put out each year in units. The same is true of the people who sell these units.

As I understand it, and I will defer to the Inspector General on this, the big problem here is one of uniformity. Not only across the board with a particular manufacturer, but even within a particular city. One dealer is getting one rebate and the other is getting another rebate, which suggests that it is not based on volume, it is based on some other criteria. But I will let the Inspector General handle that because I think he can give you more information on it.

Mr. BRYANT. Well, I wouldn't dispute what you said at all. It just seems to me that it is not good for us to leave an ambiguity in existence where you could logically argue, if you are a dealer or a manufacturer, that there is no way to determine what a small volume discount is. Apparently that is the case, there isn't any way. And I know that with regard to any litigation, or a criminal proceeding, you can't distinguish in a statute between a big manufacturer and a little manufacturer and say you are guilty because you are not big enough. It has to be more clear and more concrete than that. I wonder if that isn't the source of some of the problems here as these fellows compete with each other for business.

Mr. KANE. Well, I think there was a conscious attempt not to be too rigid in this area, to allow industry practice to have a certain influence on it and the size of the manufacturer and the dealer. But the only way to get around the problem you are suggesting, and it is a valid one, is for us to set arbitrary figures, a certain percentage of dollar sales per year or something like that, which in this day and age the Government tries to stay away from. It would be a very arbitrary situation.

Mr. O'TOOLE. Mr. Bryant, can I mention in those instances where it has been found that the manufacturer had a rebate plan and followed that plan that has not been a problem for us. It is when on an individual unit or small purchase situation, an amount has been paid to the dealer that had not been revealed in the certification.

Mr. BRYANT. Well, if I were to ask you to distinguish for me for the record a legitimate volume discount versus a small volume discount, I presume you wouldn't be able to do that; is that correct?

Mr. O'TOOLE. That is right, without knowing more about the plan.

Mr. BRYANT. Well, you define the plan and then I will ask questions about volume. I am asking about volume, not the plan. I can see why the plan is important, but my question relates to volume.

Mr. O'TOOLE. We haven't defined that.

Mr. BRYANT. Okay.

Mr. O'TOOLE. And I guess that is part of the problem.

Mr. BRYANT. Let me ask this question.

Mr. SHELBY. I wonder if the gentleman would yield one second.

Mr. BRYANT. Sure.

Mr. SHELBY. Picking up on what the gentleman from Texas has been asking you, could the regulations have been more explicit to the people dealing in the manufactured housing area?

Today you are saying that you are probaly going to look into different ways of appraising the property, therefore, do you beleive your regulations were murky?

I am not trying to make excuses for anybody. We are trying to remedy a situation and make the program work for everybody. I think that is what the gentleman from Texas was alluding to, and I appreciate him yielding. I yield back.

Would you like to respond to that? I will stay until the end. Mr. O'Toole, or Mr. Vogel?

My basic inquiry was whether or not the regulations dealing with the manufactured housing, rebates or discounts, and appraisals, could have been more explicit. VA regulations are fairly explicit when you are dealing with conventional homes. People know the rules and they know how to adhere to them. The manufactured housing group is different, as you have pointed out and I thought that is what the gentleman from Texas was alluding to.

Mr. BRYANT. That is correct.

Mr. SHELBY. Can you address that?

Mr. O'TOOLE. Well, maybe I can. In the regulations we could have spelled out what a volume rebate is.

Mr. SHELBY. That is what we are getting at.

Mr. O'TOOLE. We could have done that. But the abuses have been found—I don't think that is necessarily a good defense for those firms that are—

Mr. SHELBY. If the gentleman would yield. We are not trying to defend anybody. We are just interested in what happened, why it happened, and whether it could have been prevented. Could it have been prevented had your regulations been more explicit?

Isn't this what you are referring to, Mr. Bryant?

Mr. BRYANT. Yes, it is.

Mr. SHELBY. Thanks for yielding. I appreciate it.

Would it?

Mr. O'TOOLE. I can't answer that, Mr. Chairman.

Mr. SHELBY. Okay. But you are talking about making your regulations more explicit—the appraisal, and how you arrive at a value and everything else—are you not?

Mr. O'TOOLE. We are talking about looking at the way we determine what the value and the loan amount should be.

Mr. SHELBY. Well, you say "looking at the way," you mean you are re-evaluating—

Mr. O'TOOLE. That is right.

Mr. SHELBY [continuing]. The approach to it. So you are considering changing your regulations. It doesn't mean you will, but there is a possibility because you want the VA guaranteed loan program to work. You want to get value for value.

But to do this aren't you going to have to have explicit instructions?

Mr. O'TOOLE. Yes.

Mr. SHELBY. I thank the gentleman for yielding.

Mr. BRYANT. I just have one last question. I wonder if, when a retailer pays a lender the up front points in order to buy down a mortgage rate is it all right for the manufacturer to reimburse the retailer for those points?

Mr. O'TOOLE. I don't know the answer to that, Mr. Bryant.

Mr. KANE. The manufacturer is reimbursing the retailer for the points he paid on the money he borrowed?

Mr. BRYANT. For points he paid to a lender in order to buy down the mortgage rate.

Mr. KANE. And the manufacturer is reimbursing him?

Mr. BRYANT. Right.

Mr. KANE. Okay. The underlying issue throughout all of this, is VA paying more on its guarantee than it should?

Mr. BRYANT. Right.

Mr. KANE. That is a question we would have to see there, whether they are passing that cost on to us and the taxpayer, whereas, in effect, it is a sales promotion. And again, it is a question of how uniform it is and whether it is a regular practice. It may be legitimate. I would have to see more facts.

Mr. O'TOOLE. The minimum would be it would have to show up in the certification.

Mr. KANE. Yes.

Mr. O'TOOLE. It would have to be disclosed.

Mr. KANE. We have to know that we are paying it because our guarantee is based on that invoice.

Mr. BRYANT. Well, my understanding was that you are thinking of changing the regulations to require more disclosure. That right now your rules may not require enough disclosure. That was Mr. Vogel's testimony I think.

Mr. O'TOOLE. Yes.

Mr. VOGEL. That is right.

Mr. BRYANT. Thank you, Mr. Chairman.

Mr. SHELBY. The Chair recognizes the gentleman from West Virginia, Mr. Mollohan.

Mr. MOLLOHAN. Thank you, Mr. Chairman.

Mr. Vogel, can you identify for me, as the Veterans' Administration sees them, the problems that are associated with or targeted by the VA's Inspector General's investigation?

Mr. VOGEL. I am sorry, sir. Do you mean only with respect to the housing program, sir?

Mr. MOLLOHAN. Yes.

Mr. VOGEL. I think I would like to defer that to the Inspector General, himself, when he appears, sir.

Mr. MOLLOHAN. Well, I am just asking if you are aware of the problems.

Mr. VOGEL. In the manufactured housing? On the equity skimming sir?

Mr. MOLLOHAN. Yes.

Mr. VOGEL. Yes, sir. Yes, I am, sir.

Mr. MOLLOHAN. Could you identify them for me? Just identify the problems for the record.

Mr. VOGEL. Well, in equity skimming, a person who, of course, is a veteran—

Mr. MOLLOHAN. No, no. I am not asking you to define them. I am just asking you to identify them. You have appraisal problems. You have some accusations of kickbacks. You have some equity skimming problems. Are you aware of those?

Mr. VOGEL. Yes, sir.

Mr. MOLLOHAN. Well, will you tell me what the problems are? Will you just list them like that for me? How do you identify them? To the extent that you are aware of them, the problems that are identified or targeted and the subject of the Inspector General's investigation—could you identify them for me?

Mr. VOGEL. Pardon me, sir.

Mr. MOLLOHAN. That is really not a tough question.

Mr. VOGEL. I am going to defer to Mr. O'Toole on that.

Mr. O'TOOLE. Sir, we know that the Inspector General has an investigation going on in the manufactured housing industry and some reports of equity skimming in some parts of the country. We know on the audit side that they are working on audits on the fee appraisal system and on the VA underwriting system.

Mr. MOLLOHAN. And is that the extent of your knowledge about the subjects or subjects of their investigation?

Mr. O'TOOLE. That is all I can recall right now.

Mr. MOLLOHAN. Is that the extent of your knowledge?

Mr. O'TOOLE. Yes, sir.

Mr. VOGEL. Yes, sir.

Mr. MOLLOHAN. So you are not aware of any other matters which they are investigating?

Mr. O'TOOLE. That is right.

Mr. MOLLOHAN. How did you first become aware that those were the subjects of the investigation or become aware of those problems even before they might have been the subject of any investigation?

Mr. O'TOOLE. Well, the manufactured housing investigation was based on, in a sense, in our Atlanta office, our people in Atlanta saw some cases and thought there was a problem and referred those to the Inspector General. The equity skimming matters were referred by our regional office as a result of the servicing we do on defaulted loans. The audits on appraisal and underwriting, some of those were concerned that the—were referred to the Inspector General by the Administrator. And some items come up as part of the regular Inspector General audit of field operations and how we do things.

Mr. MOLLOHAN. Are those all?

Mr. O'TOOLE. Yes, sir.

Mr. MOLLOHAN. You have completely exhausted the problems and how you became aware of them?

Mr. O'TOOLE. Yes, sir.

Mr. MOLLOHAN. What steps, if any, have you taken to address these problems to the extent they exist, where you find them to exist, after you have looked at them?

Mr. O'TOOLE. Well, when the individual instances are pointed out to us we take whatever corrective action we think is necessary.

Mr. MOLLOHAN. In what specific way, with regard to each of the problems you have identified, did that constitute?

Mr. O'TOOLE. Well, if we want to go back to the manufactured housing—

Mr. MOLLOHAN. I want to go back to each and every one of them.

Mr. O'TOOLE. The manufactured housing situation, the agreement that we had with the Inspector General was that we would wait for more information about how the various things occurred to determine what corrective action would be necessary. Just recently we have agreed with the Inspector General that we have enough information and that we should proceed with looking at ways procedurally to change the way we do certain things in that particular program.

The issue of equity skimming is an ongoing thing. Our obligation is when we find those instances to refer them to the Inspector General for their work. And that is an ongoing thing.

Mr. SHELBY. I wonder if the gentleman would yield just for a second?

Mr. MOLLOHAN. Certainly, Mr. Chairman.

Mr. SHELBY. Mr. O'Toole, I think the committee is basically aware that there is an ongoing criminal investigation by the Justice Department and your Inspector General. I just want to make that clear. I know you are not at liberty to talk about a lot of stuff. We have a hearing Saturday in Los Angeles. Some of it will focus on equity skimming. The Justice Department and the FBI have talked to us about some of our witnesses there. Although they want us to have the hearing, they want to protect certain things for later.

Is that basically right?

Mr. O'TOOLE. That is right, Mr. Chairman.

Mr. SHELBY. You can say that here this morning without doing anything special to the gentlemen.

Excuse me. Thanks for yielding.

Mr. MOLLOHAN. That is all the questions I have, Mr. Chairman.

Mr. SHELBY. Gentlemen, thank you for coming. I am sure that we will be discussing equity skimming again. We have a number of hearings scheduled around the country. We are going to Los Angeles, and then later to New Jersey and so forth. Thank you for coming.

Mr. VOGEL. Thank you, sir.

Mr. SHELBY. Mr. Hincken, Assistant Inspector General, Office of Investigations, Veterans' Administration. Mr. Morani.

Gentlemen, as I just mentioned, we are aware there are certain investigations going on in different fields. We don't want to really get into specific details other than be aware of it. I know you have briefed me from time to time and you have briefed other members at their request.

Your written testimony will be submitted for the record in its totality. Please briefly sum up your remarks, so that we will have the time to ask questions. There are some members here who want to broadly discuss some of your investigations.

Mr. Hincken?

STATEMENT OF ROBERT HINCKEN, ASSISTANT INSPECTOR GENERAL, OFFICE OF INVESTIGATIONS, VETERANS' ADMINISTRATION; ACCOMPANIED BY RENALD P. MORANI, DEPUTY INSPECTOR GENERAL

Mr. HINCKEN. Mr. Chairman and members of the committee, I am pleased to be here today to discuss our recent investigations regarding the various types of frauds perpetrated against the VA guaranteed home loan program. As we are presently involved in rather sensitive ongoing criminal inquiries in the area, I will limit my comments to general statements on some of the types of fraudulent schemes we are encountering.

Our recent investigations have uncovered three types of fraudulent schemes that have a direct impact on the integrity of the VA's loan guaranteed program and which are victimizing veterans participating in the program. Two of the schemes involved the VA mobile home loan guarantee program, and a third scheme involves site-built homes purchased under VA loan guarantees.

The VA mobile home loan program is administered under the provisions of Section 1819 of Title 38, U.S. Code, and the 4200 series of VA regulations. Under these provisions the VA guarantees 50 percent, or $20,000, in mobile home loan amount, or whichever is less. Ninety percent of the guarantees are by automatic lenders who have authority to grant loans without prior VA approval.

During the recent fiscal years 1982 through 1984 the VA guaranteed about 37,000 mobile homes for loans totaling over $769 million. During this same period about 5,000 loans went into default and were terminated, causing the VA to pay over $36 million in default claims.

The amount of the VA guaranty is based on a manufacturer's invoice to the mobile home dealer. The VA requires the manufacturer to certify in writing that the manufacturer's invoice price reflects the dealer's cost at the point of manufacture and except for discounts based solely on volume purchases that the invoice price does not include other discounts, bonuses, refunds, rebates, prizes, or anything of value which would inure to the benefit of the dealer.

In July 1984, we initiated a nationwide investigation involving 52 mobile home manufacturers regarding a practice known in the mobile home industry as invoice padding or packing to determine if illegal rebates were occurring in the VA mobile home loan program. Our investigations have revealed that invoice padding is extensive throughout the mobile home industry and that some manufacturers include unit rebates in invoice prices in spite of the fact that they have certified they had not done so. In addition, we have determined that veterans were often charged for accessories that were not provided, and that these items were included on the invoices submitted to the VA and included in the amount guaranteed.

As a result of these practices, the VA may have overpaid an estimated $3 million on defaulted mobile home loans. As a result of our investigation to date, four manufacturers have entered negotiated guilty pleas to criminal charges and signed settlement agreements to repay the VA for its losses. Investigations involving five additional manufacturers are in the final stages.

Another fraudulent scheme that has recently come to our attention involves the resale of repossessed mobile homes. This scheme is perpetrated by individuals who are commissioned by lending institutions to resell the repossessed units. After the lending institutions repossess VA mobile homes that have gone into default the units are appraised by a VA fee basis appraiser. The repossessing agent then sells the mobile home at or near the appraised value and submits false documents showing that the home sold for considerably less than the appraised or true sales price. The VA is then asked to pay the difference between the fraudulent sales price and the veteran's indebtedness up to the amount of the VA loan guaranty.

A third type of fraud we are presently investigating involves various companies who, through fraud and misrepresentation, are acquiring title to conventionally built homes which were delinquent or in default. Our office has received a number of investigative referrals concerning alleged violations of the equity skimming section of Title 12, United States Code. The violations involve approximately 17 companies and more than 80 veterans, and potential losses to the VA in excess of $1 million.

Under an equity skimming scheme the offending company generally seeks out a veteran who is in financial difficulty and who has placed his home on the market for sale by owner. The company contacts the veteran and offers to purchase the home under certain stipulations. They offer a second trust deed as payment payable in 3 to 12 months, and also promise to pay the monthly mortgage payments until they are able to sell the property. The veteran is required to immediately vacate the property so the company can rent the house and realize some income. Income the veteran is led to believe will be applied to the mortgage payments.

When the veteran attempts to collect from the company at the end of the promissory note period, he is either stalled or ignored and eventually discovers that the company has no intention of paying the note as agreed. He also discovers that the company pocketed the rental proceeds, has made no mortgage payment on the property, and intends to let the property go into foreclosure.

Various types of equity skimming schemes have been uncovered and are under planned or active investigation. As it appears the equity skimming activities may be widespread, the Office of the Inspector General has recently published an "alert" bulletin designed to alert veterans about the equity skimming fraud and to provide them with information on how to avoid becoming victims. The bulletin has also been distributed to mortgage companies that make loans to veterans with a request from the Administrator for the companies to work with the VA in protecting the homes and equity of veterans.

Mr. Chairman, this concludes my statement.

[The statement of Robert Hincken appears at p. 63.]

Mr. SHELBY. The Chair recognizes the gentleman from Texas, Mr. Bryant.

Mr. BRYANT. Thank you, Mr. Chairman.

Mr. Hincken, you were here when I asked questions of the previous witnesses about the state of the law or regulations regarding volume discounts versus other types of rebates or small discounts.

What is your understanding with regard to the way in which the present law and regulations define a volume discount and define a small discount?

Mr. HINCKEN. There is no specific guidelines in that area, sir.

Mr. BRYANT. Do you think that has in any way contributed to the extent of—

Mr. HINCKEN. No, sir.

Mr. BRYANT [continuing]. Of apparent violation? You don't think so?

Mr. HINCKEN. No, sir.

Mr. BRYANT. Why not?

Mr. HINCKEN. What we are doing is basically just getting into the nuts and bolts of the inquiry in the mobile home area. We are looking at the companies' volume rebate plans that they have set up themselves and they are not following them.

Mr. BRYANT. You are finding instances where they are deviating from their own established plans?

Mr. HINCKEN. They are making unit rebates; yes, sir. That is why I don't believe it has any kind of significant impact.

Mr. BRYANT. Is that the case uniformly?

Mr. HINCKEN. Not everybody is packing.

Mr. BRYANT. Well, what I mean is of those who look like they may be violating the law, are they all cases where they are deviating from their stated plan?

Mr. HINCKEN. Yes, sir, the ones that we have dealt with so far to date.

Mr. BRYANT. Your testimony I think referred to 52.

Mr. HINCKEN. Fifty-one in this area; one was involved in invoicing items that veterans were not receiving. Fifty-one dealing in terms of invoice packing. Four have pled. We are now dealing with five additional corporations, and we have about 42 to go.

Mr. BRYANT. But of those, none of them, in your opinion, is a gray area. They all involve deviations from their own stated plan?

Mr. HINCKEN. Yes, sir; if they are involved in invoice packing.

Mr. BRYANT. Are there arguments with regard to what their plans actually mean?

Mr. HINCKEN. If we run into a problem as to whether or not it is a reasonable plan, we defer to counsel and the program people to make a determination. But it is generally a common sense approach, sir. If you are only selling one mobile home to one dealership three States away, and you give him a $1,000 rebate, it is clearly a unit rebate. He has never bought another mobile home from you in the past, he buys one a year—I mean it is clear that they are violating the statute.

Mr. BRYANT. Are most cases like that one, as aggravated as that one, or as clear as that one?

Mr. HINCKEN. Yes, sir. In going through this process, we are spending a great deal of time with corporations and corporate

books, going through and covering all of their activity. We are basically down to telling them here is our position. We listen to what they have to say; and for those questionable calls, we are getting counsel's and program people's guidance as to whether it is valid or not, and we will go with it one way or the other. We will drop it or we will move forward.

Mr. BRYANT. Well, you heard me ask the question at the end a moment ago probably about the reimbursement of points. Is the reimbursement of points by a manufacturer or retailer okay when the retailer pays a lender up front points?

Mr. HINCKEN. That is a program area, sir; I would let the program people answer that question.

Mr. BRYANT. Okay, well, explain to me why that is not in your area.

Mr. HINCKEN. We are looking at the unit rebates in terms of false certification on kickbacks or packing; rebating money to the dealers through their sales program. We are not looking at the financing area at all.

Mr. BRYANT. Well, no. But that is my question, though. If a manufacturer rebates to a retailer points that the retailer paid to the lender in order to buy down the mortgage, would that fall within the category of——

Mr. HINCKEN. I think it is a close call, either way. I could sit here and tell you that it may in fact violate the certification, or the intent of the certification, and there may be an argument the other way as well. I am not familiar with those.

Mr. BRYANT. Okay. Thank you, Mr. Chairman.

Mr. SHELBY. The Chair recognizes the gentleman from West Virginia, Mr. Mollohan.

Mr. MOLLOHAN. Thank you, Mr. Chairman.

How widespread, Mr. Hincken, are these kickback schemes, equity skimming schemes, and fee basis appraisal problems?

Mr. HINCKEN. Can we take them one at a time, sir?

Mr. MOLLOHAN. Please.

Mr. HINCKEN. Okay. In talking in terms of the mobile home, as I stated not everybody is involved in invoice padding, there are corporations that are not engaged in that activity.

Mr. MOLLOHAN. Is it a nationwide problem?

Mr. HINCKEN. It is extensive in the industry.

Mr. MOLLOHAN. To what extent are you in your investigation? How far along?

Mr. HINCKEN. We essentially have closed, or will be closing shortly, nine matters. We will be dealing with 42 more, who we are now presently engaged in discussions with, and in a review of their books and records. Also they are making returns on subpenas. So we are in various stages with 42 additional manufacturers, some of whom have not been rebating and we will make those calls as we see them.

Mr. MOLLOHAN. And is this a nationwide investigation?

Mr. HINCKEN. Yes, sir. As I say, it is 51 manufacturers and it is very representative of the industry.

Equity skimming is another matter that is growing by the day or by the week. In working with the regional office people we are getting referrals. We have at this point some 17 corporations targeted

or under investigation, some 80 guarantees, and we are looking at probably a cost of $1 million. These numbers change on a daily or weekly basis. As we become more sophisticated in picking it up, as the "alert" bulletins are getting out, people become aware of the scenario, and we are getting greater feedback from the regional offices.

Mr. MOLLOHAN. When did you start your investigation?

Mr. HINCKEN. Which one, sir?

Mr. MOLLOHAN. Well, when did you start the first investigation, and what was it, into the problems that you are just identifying right here—kickback schemes, equity skimming schemes, and the fee basis appraisal problems in the VA program?

Mr. HINCKEN. On the equity skimming matter I believe—I don't have the precise dates here but I don't mind estimating. That would have been about October 1984, in California, where we first ran across the problem.

Mr. MOLLOHAN. And when you were first called in to investigate it?

Mr. HINCKEN. Right about that time, yes, sir. That is when the regional office had picked up some rather unusual foreclosure situations and veterans complained about a contract they had signed that was not enforceable. We got into the matter at that time with the Long Beach Police Department and a special prosecutor. The matter has subsequently been raised up to the Federal level with the United States Attorney and the Department of Justice in California.

Mr. MOLLOHAN. What is the regional office, did you say?

Mr. HINCKEN. The Home Loan Guarantee Division at the VA regional office there.

Mr. MOLLOHAN. What different things are you investigating? If you were just to categorize them, what different problems are the subject of your investigation? To the extent that you feel free to disclose it here.

Mr. HINCKEN. Well, we are looking at mobile homes on the front end and on the back side of that, if you will, repossession. We are looking at home loan guaranty in a number of areas. We are looking at equity skimming in seven or eight major metropolitan areas. We are also looking at loan guaranty problems in Camden and Willingboro. In Camden it is essentially a HUD problem and we are assisting there. We are also actively engaged in several other locations in New Jersey.

The problems we are finding have resulted in some heads up notices to management; we have got some credit reporting problems; we have got falsification of applications. These are the kinds of problems that we are encountering. False bank account information. Schemes that are set up by various people to get eligible—excuse me—to create eligibility for a certain class of people who really could not afford the property. That is ongoing in a number of areas.

Mr. MOLLOHAN. And each one of these problems that you are identifying, are you still involved in the investigations?

Mr. HINCKEN. Yes, sir.

Mr. MOLLOHAN. And some of them you have been picked up along the line? I suppose you have picked up different problems. As

you are investigating one, you have picked up another one, so you are at different stages in the investigation with regard to each one?

Mr. HINCKEN. Right. As we go along, and obviously we have been at this now for about 7 or 8 months with a large investment of time and effort, and we have acquired more knowledge. We hope we will be able to target problem areas and move in quickly, in the future.

Mr. MOLLOHAN. The DAV in their testimony quoted an August 12, 1985 Forbes article which states:

"A VA Insider estimates that one-third of the 25,000 foreclosures last year involved some sort of fraud ranging from falsification of homebuyer's creditworthiness to over valuation of properties."

Based on your investigation to date, if you feel at liberty to disclose it, do you feel that this is an accurate estimation?

Mr. HINCKEN. It is probably too early in our efforts to come out and say one-third, or give it any kind of percentage. My gut reaction at this time is to characterize the situation as extensive, sir, but I really could not say it is 10, 15 or 20 percent. We have a long way to go. These are very complex, time-consuming matters and to get a feel on it we are going to have to be around the country in a number of areas. I just don't think Willingboro, NJ, is representative of the rest of the country.

Mr. MOLLOHAN. One last question, Mr. Chairman, please.

So far you have discussed here various schemes—kickbacks, fraudulent appraisals, et cetera—from outside the Veterans' Administration. Do you have any evidence that would indicate that VA employees may have contributed or participated in any of these illegal activities?

Again, if you feel it would be appropriate for you to disclose that.

Mr. HINCKEN. I would like to defer on that, sir, and just not even get into that area, if I could, please.

Mr. MOLLOHAN. Thank you, Mr. Chairman.

Mr. SHELBY. Mr. Hincken, have you had pretty good cooperation from the manufactured housing people?

Mr. HINCKEN. As an industry across the board, yes, sir. We have had discussions with them for a period of time. I know that they are involved in trying to formulate a new evaluation system.

Mr. SHELBY. Similar to what Mr. O'Toole and Mr. Vogel talked about?

Mr. HINCKEN. Yes, sir. Discussions are at least underway. They are having their system evaluated by the Antitrust Division of the Department of Justice.

Mr. SHELBY. Do you have any recommendations that you might want to submit to the committee—if not now, in writing—that would bring about a streamlined effort on evaluation, discounts, and rebates, and so forth, in other words, how to avoid problems in the future?

Mr. HINCKEN. Yes, sir. We are in the process of analyzing and reviewing, and we would like to discuss it with the Department, Mr. Vogel and Mr. O'Toole, and give them our perspective.

Mr. SHELBY. Would you share that with members of this committee and subcommittee?

Mr. HINCKEN. Yes, sir.

Mr. SHELBY. Was there a murky area there? Could it have been more explicit, as some of us have alluded to; or is it clearcut, or what?

Mr. HINCKEN. Well, as Mr. Kane and Mr. O'Toole enumerated, they were letting the industry practice and the industry habits in selling carry the day, if you will, which appears to be fine. As I said earlier, the companies had their own plans and were ignoring them. So they knew what a volume rebate was; they had set up their own plans. So to suggest that they didn't know, when in fact they violated their own internal policies or procedures.

Mr. SHELBY. I know you mentioned that this was widespread in the industry. What do you foresee as the outcome of this? I know it is an ongoing deal, some positive things?

Mr. HINCKEN. Yes, sir. Absolutely, very positive. I think that we will clear up this matter—and we are addressing it as quickly as we can. I assume we will come out with a new procedure, a new policy, and a strengthened manufactured home program where everybody understands the ground rules.

Mr. SHELBY. How long do you foresee it would take to clear it all up?

Mr. HINCKEN. Sometime in 1986, sir. Unless of course the cooperation level drops off. Then we must proceed to district courts or subpoena enforcement actions. There are a number of options.

Mr. SHELBY. Thank you.

Counsel?

Thank you, gentlemen. We want to keep the record open for some written questions we might have to you.

Mr. HINCKEN. Yes, sir.

Mr. SHELBY. Our next panel is Mr. Jerry Connors, president of Manufactured Housing Institute, and he is accompanied by counsel and vice president, Finance, Mr. Weiner and Mr. Joseph Owens; Mr. Will Ehrle, president and general counsel, Texas Manufactured Housing Association, accompanied by Mr. William Beville, who is chairman, National Manufactured Housing Federation; and also Mr. Danny Ghorbani, president, Association for Regulatory Reform.

Gentlemen, please come on up to the witness table. Your written testimony, as you know, will be submitted to the record in its totality without objection. Since we are pushed for time today, please briefly sum up your oral testimony as this will enable us to ask you questions.

Mr. Connors?

STATEMENTS OF JERRY C. CONNORS, PRESIDENT, MANUFACTURED HOUSING INSTITUTE, ACCOMPANIED BY HARVEY WEINER, COUNSEL, AND JOSEPH OWENS, VICE PRESIDENT, FINANCE; WILL EHRLE, PRESIDENT AND GENERAL COUNSEL, TEXAS MANUFACTURED HOUSING FEDERATION, ACCOMPANIED BY WILLIAM D. BEVILLE, CHAIRMAN, NATIONAL MANUFACTURED HOUSING FEDERATION; AND DANNY D. GHORBANI, PRESIDENT, ASSOCIATION FOR REGULATORY REFORM, ACCOMPANIED BY EDWARD F. CANFIELD, ESQUIRE

STATEMENT OF JERRY C. CONNOR

Mr. CONNORS. Thank you, Mr. Chairman. I am Jerry Connors, president of the Manufactured Housing Institute, and I will try to summarize my remarks.

We, in the manufactured housing industry believe that the VA Home Loan Guaranty Program has been beneficial to veterans. Almost 97,000 veterans have purchased manufactured homes under this program in the 15 years it has been in effect. The program has allowed these veterans to purchase safe, affordable and durable housing.

We are, of course, aware of the VA Inspector General's current investigation related to invoicing practices in our industry. We are also aware of the news reports that have unfairly characterized completely legal business strategies and totally distorted the dimensions of the situation. In fact, much of the controversy has been brought about by a misunderstanding of the entirely appropriate role of volume incentive plans. The manufacturers in this industry, as is the case in many other industries, employ these plans as marketing tools. The way the VA certification was drafted, in fact, gave wide latitude to manufacturers in creating these programs.

Volume incentive plans were not created and are not used to defraud veterans, but are, in fact, an entirely appropriate, commonplace and legal marketing tool. Our testimony contains several charts which document how one of these plans might work. These examples show clearly that the veteran has not been damaged through the use of volume incentive plans. In rare cases illegal programs may have been employed. We in no way condone these actions. We reiterate, however, our belief that illegal activity is extremely limited.

We further submit that the focus should be on a revision of the VA regulations to eliminate the vagueness that currently exists and to structure a program that gives the industry clear guidelines. The industry has already moved, as Mr. Hincken pointed out, to set up a framework to more clearly define and categorize various types of volume incentive plans. We were pleased to learn that the VA now plans to move forward on a revision of the regulations that govern this program. We look forward to working with the VA on these efforts.

Thank you, Mr. Chairman.

[The statement of Jerry C. Connors appears at p. 67.]

Mr. SHELBY. Mr. Ehrle?

STATEMENT OF WILL EHRLE

Mr. EHRLE. My name is Will Ehrle. I am president and general counsel of the Texas Manufactured Housing Association. Accompanying me today is William Beville. He is not at the table, but he is here for any particular questions for him. He is a retailer engaged in the manufactured housing business and is chairman of the National Manufactured Housing Federation, on whose behalf we speak today.

In summary of my written testimony, Mr. Chairman, I would like to refer to the conclusions and recommendations and get to the heart of the matter.

Mr. SHELBY. You may proceed.

Mr. EHRLE. We commend the Veterans' Administration and the Congress for establishing this program. We think it has been a marvelous program for the almost 100,000 veterans in this country that otherwise might not have had a home of their own. We regret the unfortunate publicity, frankly, that has implied that kickbacks and illegal invoice padding practices are widespread in the industry, and I will comment a little more on that a little bit later.

We emphasize very, very strongly that the present Veterans' Administration regulations do not differentiate between volume discounts which are legitimate, which are authorized under the regulations, which are authorized in their circular, and which, by the way, the Robinson-Patman Act specifically recognizes as a way of doing business within the fair competitive realm in this country. Without specificity in an extremely competitive atmosphere, how is a manufacturer or retailer, without definitive rules, to know what to do?

The Inspector General mentioned this morning that, gee, if they had just followed their own plans, well, then everything is fine. Well, super. That is great and I agree with that. What are we talking about, though? Let us say, through an administrative or clerical error, or some problem, like changeover in personnel, we have three deviations, five deviations in a plan out of large numbers. Is that a deviation or a failure to follow the plan? It is a criminal activity? It is an illegal pad in an invoice? I think not. I think not. And I do not believe a court in this country is going to find so, either.

Legitimate volume discounts are not kickbacks, they are not rebates, and even if there were an error in administration in a company that does not make it illegal. It may be negligent, but it is not illegal.

There are special rebates that frankly don't injure the veteran. Those kinds of rebates under the certification should be disclosed. I know of no single manufacturer in this country or no example where a lender that is an automatic lender for the VA program has ever requested definitive information from a manufacturer on rebates when that information wasn't given. The vast majority of the current repossessions, Mr. Chairman, are without question a result of the economic conditions in this country.

Now, frankly, whatever we want to say from a public standpoint, the economy is the culprit, the economy is the guilty party. This country is not in good shape, and that is particularly true in States

such as Texas, Oklahoma, Louisiana, and others that particularly are heavy into the energy areas. It is certainly true with farming and ranching. It is certainly true with many other industries in this country today. So that is the problem with repossessions, both with site-built structures as well as with manufactured homes.

Volume discounts, rebates, small volumes—yes. What is small volumes? Sure it is single units, I understand. Everybody can comprehend that. But small volumes—is that three units? Is it five units ? Is it $100,000? $500,000? And to say that it would be arbitrary to make the regs specific is absolutely ludicrous when the regs are specific to the point of saying 120 percent of the manufacturer's invoice. Why couldn't the regs have specified some particular maximum percentage for any kind of a lawful, legal rebate? If there has been a problem, why has this not been addressed by the Veterans' Administration? And I just don't think it is right for folks to, in effect, be accused of criminal conduct because of competitive practices within an industry that have not violated the specifics of the regulations.

Mr. Chairman, I appreciate an opportunity to present the written testimony. We would be more than happy to answer—I am sorry Mr. Bryant has gone because he asked me a bunch of questions yesterday and didn't get to finish, but we would be glad to respond in writing to any questions that any member of the subcommittee might have, and of course we will be available to answer questions in a moment.

Mr. SHELBY. Thank you.

[The statement of Will Ehrle appears at p. 84.]

Mr. SHELBY. Mr. Ghorbani?

Mr. GHORBANI. Yes, sir.

Mr. SHELBY. Go ahead.

STATEMENT OF DANNY D. GHORBANI

Mr. GHORBANI. Mr. Chairman, members of the committee, my name is Danny Ghorbani, and I am the president of Association for Regulatory Reform.

Our Association was formed this past July to represent the interests and views of the manufacturers of manufactured homes. Our membership is comprised of manufacturers only.

The purpose of my testimony today is to discuss the subject of Veterans' Administration's guaranteed manufactured home loan and the related subject of alleged industrywide invoice irregularities.

Although ARR's position is explained in detail in our written comments submitted to the subcommittee earlier, I would like to briefly summarize a view which has been largely ignored in the midst of the current allegations of industrywide fraud. In short, that view is that, while invoice irregularies might have existed in some individual cases, the manufactured housing industry by and large has not engaged in illegal or questionable practices. Our position is quite different from the ones you have heard so far, and the four components of it includes, as follows:

1. The VA certification requirement, which was published informally in a VA circular letter without an opportunity for comments

and without explanation, is ambiguous and confusing and not properly the basis for criminal prosecution.

2. Most manufacturer invoices do comply with the requirements of the certification when that certification is understood in the context of Veterans' Administration's stated purpose for issuing that circular. That purpose, the way we understand it from the documents that we have obtained, was to prevent dual pricing practices in the Veterans' Administration manufactured home program because veterans should not—and we agree with this—be charged a different price than other purchasers.

3. Industry invoicing practices which recently have been alleged to constitute illegal rebates are not illegal because they do not result in dual pricing. Moreover, the concept of rebate, current in the industry when the circular letter was issued, was different than the meaning now attributed to the word by the VA. For example, the invoicing code agreed upon by the industry at the time defined a rebate as an attempt to increase the invoice above list price with a return of the excess to the dealer.

4. The invoice practices which are now construed as improper, and they have been tacitly approved thousands of times by VA during the 6-year period in which the certification has been in effect. These invoicing practices, which are permitted in every major industry, should not now, on the basis of an ambiguous certification, be used to justify allegations of fraud against an entire industry.

We believe that the VA has done a splendid job of supporting ownership of homes for veterans. Either high interest rates and pressure from lenders due to the high rate of default in all housing have caused a tense situation in which we feel analysis and judgment have been very hurried. We suggest that the facts do not warrant the indictment of the entire industry. Our research, in detail, has been presented to you earlier.

With me here today is Mr. Ed Canfield, who is the General Counsel of our Association. He is here somewhere if we need him. And I would be happy to answer any questions you might have.

Mr. SHELBY. Thank you.

[The statement of Danny D. Ghorbani appears at p. 111.]

Mr. SHELBY. I appreciate your abbreviating your statement.

I have several questions. Mr. Ehrle or Mr. Connors, you heard the testimony earlier from Mr. O'Toole, Mr. Vogel, and the Inspector General. What we were trying to do is to get everyone back on track.

Were the VA regulations not explicit? I know that there are volume discounts in automobiles, trucks, appliances, et cetera. I understand that. It is just the way that people do business. Incentives to do business. If I were General Electric, for example, and I were selling refrigerators and stoves, et cetera. I would have to give incentives for people to do business with me, or with my firm.

Is this where discounts came about, Mr. Ehrle? Is this just part of the manufactured housing business which occurred before the industry got into VA programs?

Mr. EHRLE. Yes, sir, it is; and as a matter of fact, your example was an excellent one. All appliance manufacturers have graduated tiers of pricing. There has been a lot of case law as to whether

those manufacturers could sell at different prices because of quantity.

Mr. SHELBY. That has been held up, hasn't it, in courts?

Mr. EHRLE. Yes, sir, it certainly has. The large volume discount stores, can they buy cheaper than the "mom and pop" corner operator in the small town? The courts have said yes. Volume-related discounts are perfectly valid.

Mr. SHELBY. Let us go into the financing area. Do some of the banks and financial houses that finance cars, finance different things, appliances and so forth, you know, you do so much business with them and, if there is very few repossessions or foreclosures, whatever you want to call them; don't they then either give you a discount, or rebate on your interest rate, or a cash rebate if you carry so much paper with them over so many years? Are you familiar with that?

Mr. EHRLE. Mr. Chairman, I would have to say that from a hearsay standpoint I think that is certainly true in a number of industries. That particular aspect really has not been prevalent in the manufactured housing picture.

Mr. SHELBY. Well, I wasn't talking about manufactured housing. I am talking about just in general business, say, automobiles.

Mr. EHRLE. Well, yes, sir. Certainly that is my understanding. Of course there is a difference in that most of those loans are not made based strictly on a percentage of the invoice cost. So there would be a difference, perhaps, in that. Yes.

Mr. SHELBY. Mr. O'Toole and Mr. Vogel also alluded to, after questioning by myself and some of the other members, that they were going to try to work out some specific regulations regarding how you valuate a manufactured housing unit.

Would your organizations cooperate with them on this? I know, they even admitted here at the table that it was different from valuating a "stick" built house.

Mr. CONNORS. Well, Mr. Chairman, during the course of the VA investigation we have tried on several occasions to meet with the VA program people to begin negotiations to revise the program to add some clarity. Up until recently that has not been possible because the Inspector General has asked that no negotiations begin. As he pointed out, and as the program people pointed out, that prohibition has now been lifted, and we hope to work very closely with them.

Also, as Mr. Hincken pointed out, we have put together a truth-in-invoicing-practices statement which we think will form the framework of a very adequate program.

Mr. EHRLE. The National Federation certainly would join the Manufactured Housing Institute in that cooperative effort.

Mr. SHELBY. Well, that is what we are really interested in, is making the program work, isn't it?

The gentleman from Tennessee, Mr. Sundquist.

Mr. SUNDQUIST. Thank you, Mr. Chairman. I understand what you say in your testimony in terms of sometimes the word "rebate" should be used instead of some other terms, and I have appreciation for the media sometimes using one instead of the other.

How many manufacturers do we have in your business? How many exist—the majors—in the country?

Mr. CONNORS. Well, majors?

Mr. SUNDQUIST. Well, majors or—

Mr. CONNORS. Well, there are about 170 companies, but many of those 170 are small. If you are talking about majors, it is more in the range of 50.

Mr. SUNDQUIST. Mr. Ehrle, from your testimony, you don't think the problem that we have is a major problem?

Mr. EHRLE. No, sir, I honestly do not. Certainly there are examples, and there have been people that have pled guilty. And I would certainly assume that the corporations did not do that unless they felt jeopardized to some extent. But we certainly don't condone putting items on an invoice that are not delivered to the veteran. That is fraud. We certainly don't condone having two sets of invoices, one for some dealers and other invoices at a higher rate on the same home for other retailers. That is obviously fraud and it is not condoned.

But I am saying that I think those practices are rather limited. The widespread practice is the one of the various marketing incentive plans that are based, at least to some extent, on volume.

Mr. SUNDQUIST. I have no problem—I guess the problem comes in definition and enforcement. On the other hand, back in April of this year in the Wall Street Journal, titled "Veterans Group Sues Six Makers of Mobile Homes," it mentions in there that since February three mobile home manufacturers have pleaded guilty to making false certifications and have agreed to criminal fines, et cetera, et cetera . . . about 50 others, representing half of the Nation's major mobile home producers, are negotiating blank settlements including guilty pleas to criminal charges.

Mr. SUNDQUIST. What has happened since then, and is it that widespread?

Mr. CONNORS. No, we do not believe it is that widespread. As Mr. Hincken pointed out, he is in the early stages of the investigation in terms of making his way through the 52 manufacturers that he described.

The basic problem with those kinds of numbers and the kind of publicity that has been generated is, going back to the vagueness of the certification, many, many of the manufacturers in the 52 don't honestly feel that they have any kind of a problem with the Veterans' Administration certification. But again, because of the vagueness, it is very unclear. And these people, because of the way the Veterans' Administration began and approached the investigation, felt it incumbent upon them to contact the Veterans' Administration to ascertain what the Veterans' Administration was after and what their position was with respect to the Veterans' Administration.

Mr. SUNDQUIST. We certainly don't want to impugn an ongoing industry, but at the same time we appreciate your testimony and your input as to how we can clarify it so that there is no question about confusing padding or kickbacks or double invoicing or not delivering on certain items within a manufactured home when they are listed. I mean, we have to eliminate that somehow and your continued assistance in that will be appreciated.

Thank you, Mr. Chairman.

Mr. SHELBY. Thank you.

I have an observation, maybe a question. Mr. Connors, let us discuss X, a company which manufactures these mobile homes. Is it a practice in the industry, or was it a practice, to offer a discount or rebate, on every mobile home regardless of financing? For example, let us say I come in and I buy a manufactured home from a dealer for cash. Would the dealer still get the rebate or the discount or is that just for VA loans?

Mr. CONNORS. Oh, no, not just for VA loans.

Mr. SHELBY. It's for everything?

Mr. CONNORS. Yes. Volume incentive plan—

Mr. SHELBY. In other words, your practices aren't singled out just for the VA, is it?

Mr. CONNORS. No.

Mr. SHELBY. Okay, one set of rules for everybody?

Mr. EHRLE. Mr. Chairman, could I comment briefly on that?

Mr. SHELBY. Yes, sir. Go ahead, Mr. Ehrle. You see what I am getting at?

Mr. EHRLE. Oh, yes, sir. At the retail level, let me emphasize that the vast, vast majority of the time, unless that retailer is sitting next to a military base, when that customer comes in and they look at homes they talk price. That retailer does not know that individual is a veteran, and unless they get very close to a price, financing is never even discussed.

Mr. SHELBY. What percentage of the manufactured housing, roughly, is financed through the Veterans' Administration?

Mr. GHORBANI. It is around 3 percent.

Mr. WEINER. 3 to 5 percent.

Mr. SHELBY. How much?

Mr. GHORBANI. 3 to 5 percent.

Mr. SHELBY. 5 percent?

Mr. GHORBANI. 3 to 5 percent.

Mr. SHELBY. That would be a small amount?

How much would be financed through HUD?

Mr. WEINER. Approximately, it depends on the year, but at various times as much as 10 percent.

Mr. SHELBY. So between VA programs and the HUD programs, you are talking about maybe 15 percent.

Mr. WEINER. Yes, sir.

Mr. SHELBY. And then the other 85 percent of the financing of the homes would be cash or conventional financing. And the discount or rebate would appear regardless of who financed it? If it was cash, if it was CIT, if it was Bank America, or the veterans' guaranteed loan, you name it, it is the same basic thing?

Mr. CONNORS. Yes, Mr. Chairman.

Mr. SHELBY. Okay.

The gentleman from Tennessee.

Mr. SUNDQUIST. Thank you. If you would yield, Mr. Chairman, I would appreciate it, for one question I neglected to ask of Mr. Connors.

Mr. Connors, on page 9 of your written testimony you state that the Institute has developed a truth-in-invoice-practice statement. Could you just briefly expand on the purpose of the statement, and what its status is?

Mr. CONNORS. Well, the purpose of the statement is to add clarity to this entire situation with volume incentive plans whether it be with respect to VA guaranteed loans or any other kind of loan. Basically, it is a combination of certification and disclosure. Certification to the lender or the guarantor of the types of volume incentive plans a particular manufacturer would have, and disclosure of any rebates that do not fit in with that plan.

Mr. SUNDQUIST. Thank you, Mr. Connors. Thank you, Mr. Chairman.

Mr. SHELBY. I thank you, gentlemen, for coming and appearing. If we have any questions we will submit them to you in writing. Thank you, gentlemen.

Mr. SHELBY. Our next panel is Mr. Ronnie Wynn, Mortgage Bankers of America; Mr. Burton Wood will accompany him, legislative counsel; and Sharon Canavan. We also have Ms. Dorcas Helfant, national vice president, National Association of Realtors.

Ms. Helfant, yours and Mr. Wynn's testimony will be made a part of the record without objection. If you will, please briefly sum up your testimony in this hearing. You may proceed, ma'am.

STATEMENTS OF RONNIE WYNN, PRESIDENT, MORTGAGE BANKERS OF AMERICA, ACCOMPANIED BY BURTON C. WOOD, LEGISLATIVE COUNSEL, AND SHARON M. CANAVAN, DEPUTY LEGISLATIVE COUNSEL; AND DORCAS T. HELFANT, NATIONAL VICE PRESIDENT, NATIONAL ASSOCIATION OF REALTORS

STATEMENT OF DORCAS T. HELFANT

Ms. HELFANT. Thank you. I am a realtor from Virginia Beach, VA, which has one of the largest military populations in the Nation, and I serve as the regional vice president and will be in 1986 vice president of the National Association of Realtors. I was also appointed to chair our association's Veterans' Administration Housing Program Task Force.

On behalf of the more than 670,000 members of the National Association of Realtors and our NAR president, Dave Roberts of Mobile, AL, I want to thank the Chair, Representative Shelby, and members of the subcommittee for the opportunity to appear here today.

Realtors feel we can help the Veterans' Administration keep the costs down of the VA Home Loan Guaranty Program in order to maintain this important veterans' benefit. Before I present to the subcommittee the recommendations of our task force which were recently adopted by our association's executive committee, I would like to thank both the Veterans' Administration and the congressional staff members for giving us their time and assistance in our project.

During the course of this past year the financial problems of the VA revolving fund and the administration's proposed increase of the current 1 percent user fee have encouraged the National Association of Realtors to study and review the VA Home Loan Guaranty Program in general, and more specifically the management and disposition of the inventoried properties. Earlier this year, a group of realtors met with the Veterans' Administration staff to

discuss the various procedures of the VA Home Loan Guaranty Program. The realtor members made the following general recommendations on improving the operations of the system:

Strengthen and standardize underwriting guidelines.

Implement a review process for quality control of appraisals and continue to implement a case-by-case foreclosure policy.

Recognizing that prior to the enactment of the Deficit Reduction Act of 1984 perhaps the single most expensive drain on the VA revolving fund was the excessive volume of VA foreclosures, the National Association of Realtors supported congressional legislation last session to institute a case-by-case economic benefits foreclosure policy. The realtor group concluded that the Revolving Fund's current financial deficit could be best assisted by the sale of its inventoried properties which reached a high point this year of approximately 22,000 with an estimated worth of $800 million. Given the expertise of the real estate professional, the realtor group recommended that the National Association of Realtors concentrate its attention on this financially burdensome inventory.

In August a second group of realtors met with the sole objective to devise a model program to dispose and manage the VA inventoried properties. The task force successfully designed a marketing program which it later reviewed and discussed with the VA staff and House and Senate Veterans' Affairs staff. The main purpose of the marketing program was to develop a system using the realtor structure which would inform the real estate professional of the VA inventoried properties and encourage their participation in the program. The plan also sought to generate better communications among the local VA staff and the real estate professional and the potential homebuyer.

The marketing plan envisioned the participation of either a realtor local board or State association in presenting to VA a flexible plan to assist in the disposition of VA inventoried properties. The appropriate realtor organization would either create or make use of an existing information service or system. This system would provide interested real estate professionals within a specified geographic area with necessary data to evaluate the available VA properties so as to accommodate the prospective homebuyer with another option.

This new information system would provide VA with a broader, more industry compatible marketing tool. The information would be delivered to the real estate professional on a cost-plus differential fee basis with each realtor organization negotiating the system's cost with the appropriate VA regional office. The realtor organization would also provide the real estate professional with all necessary VA forms as supplied by VA.

In addition to the information system, a liaison component between the realtor organization and the VA regional office was felt to be essential to the success of the marketing plan. Therefore, a VA advisory council would be created at the appropriate system level which would be comprised of local real estate professionals and VA regional staff. The council would assist VA with the pricing of its properties based on market data, the marketing of its properties, and the development of education programs which would be made available to interested licensees and which would

explain the VA process and illustrate how to effectively market the program.

I have other testimony that is written for the record and comments on Congressman Sundquist's bill. But in the interest of time, thank you, sir.

Mr. SHELBY. That will be included in the record in its totality.

[The statement of Dorcas T. Helfant appears at p. 138.]

Mr. SHELBY. Mr. Wynn?

STATEMENT OF RONNIE J. WYNN

Mr. WYNN. Mr. Chairman, I am president of Colonial Mortgage Co. of Montgomery, AL, and also vice chairman of the legislative committee of the Mortgage Bankers Association of America. MBA appreciates the opportunity to appear before you today to testify on the VA's Home Loan Guaranty Program.

I would like to thank the chairman and the subcommittee members for your support in rejecting any increase in the VA funding or user fee as proposed by the administration. Your opposition to such an increase was most helpful in defeating that proposal during the consideration of the fiscal year 1986 budget resolution.

It may well be that new taxes will be necessary to allow the Government to reduce the Federal budget deficit, but those taxes should be broad based and should be decided upon in an open discussion of tax policy. The 5 percent user fee proposal constituted a "back door" levy on homebuying veterans thinly disguised as a cost-related user fee intended to strengthen the program.

The VA Home Loan Guaranty Program is currently undergoing a review of its scope and administration particularly because of its recent losses. Such an analysis is worthwhile but should not lose sight of the original purpose of the program, which is to provide an entitlement benefit designed to assist veterans to purchase a home.

An MBA task force recently completed a report containing a number of suggested improvements that, if implemented, would diminish losses. Many defaults can be tied to lax origination, underwriting and appraisal standards. While the intent of the VA Home Loan Guaranty Program is to expand the mortgage credit opportunities of veterans, it is a disservice to a borrower to extend credit where the borrower's default may be likely.

The report focuses on improved standards including more stringent housing expense-to-income underwriting guidelines, restriction of access to VA field offices to reduce pressure for approvals, identification of loans that are being resubmitted for approval to tag potential problems. Lenders' underwriters should develop expertise in appraisal underwriting and apply that expertise to VA appraisal. A standard appraisal form should be developed for use by VA, FHA, Fannie Mae and Freddie Mac. VA should consider allowing lenders to select appraisers. VA should develop a system to identify appraisers who perform the original appraisal on all foreclosed properties in order to determine if those properties that end in foreclosure consistently have significantly lower values at the time of foreclosure than at the time of origination.

The task force also recommended changes in servicing and foreclosure procedures that were designed to minimize program losses.

VA has responded to MBA's report, and MBA will provide its analysis of that response for inclusion in the hearing record.[1]

H.R. 2801 would authorize VA to establish a program where VA-held properties would be sold at a discount. MBA is concerned that greater losses resulting from discounted sales would further fuel the effort to impose larger user fees on veteran borrowers. In order to move its inventory, VA should place more emphasis on pricing homes at their market value. Rather than an automatic sales price discount, VA should review its assigned price after a certain time limit. VA should look at comparable sales prices or even order an updated appraisal to confirm that the assigned price is a fair market value.

MBA supports an increase in the maximum guaranty amount of the VA loan from the current $27,500. Had the VA maximum guaranty been adjusted annually in equal proportion to the increase in new home prices the 1984 guaranty would have reached $39,000.

Under current law the maximum interest rate allowable on a mortgage guaranteed by the VA is fixed by the VA Administrator. MBA has consistently urged that the law be amended to allow interest rates to be determined by the market. MBA urges that the VA be authorized to include adjustable rate mortgages, or ARMs, in the home loan guaranty program. ARMs are a beneficial development that permits borrowers and lenders to tailor transactions to the needs of the borrowers.

We appreciate the opportunity to appear before the subcommittee today, and we will be pleased to furnish any additional information or answer any questions you may have. Thank you.

Mr. SUNDQUIST [presiding]. Thank you, Mr. Wynn.

[The statement of Ronnie Wynn appears at p. 144.]

Mr. SUNDQUIST. I should tell you that our distinguished chairman went over to vote and will be back shortly. We do not have revolution in the committee.

[Laughter.]

Mr. SUNDQUIST. Is there further testimony? Ms. Helfant, we heard from you and Mr. Wynn. Mr. Wynn is associated with some good friends of mine down in Alabama. Appreciate you being here today.

Mr. WYNN. Thank you, sir.

Mr. SUNDQUIST. The question I have refers to your testimony about the VA Home Loan Guaranty Program, on page 2.

Mr. WYNN. Yes, sir.

Mr. SUNDQUIST. You reaffirm that this is a program for veterans, and we ought to help veterans. One of your objections, as I understand it, is that it looks like my legislation would be mandated. It is not. It gives the Administrator the option of using that.

Would you care to comment on that, Mr. Wynn?

Mr. WYNN. Well, we certainly appreciate you clarifying our misunderstanding as to whether it is a mandate or not. However, we would suggest that a proposal of this type needs to be carefully studied in light of some of the early testimony and some of the earlier questions that were being posed to the VA. As it pertains to what savings could be achieved and to our concerns that the price be the market price. Under your bill our concern is that it would

[1] See p. 248.

eventually become an automatic thing that veterans would not become involved until such time as the VA discounted sales price reached the minimum level of pricing.

Mr. SUNDQUIST. Well, I understand your concern. That would not be my intention. The market value ought to be the price. I am afraid that the price we have is way above market in many instances.

Mr. WYNN. We certainly would not agree with properties being priced above market value because it accomplishes nothing and, in fact, does increase costs if that is the case. Because certainly the market is going to determine what the property will sell for.

Mr. SUNDQUIST. And if, in fact, we are spending some $70 million a year in interest rates on our inventory, it is not hard to figure out why we have had to go back for more money from the Congress on that fund. And it seems to me that we have got to do a better job of managing. When it has been held for some 30 months, we have to take into account what it is going to take to put it back in place or perhaps the price is too high.

These are questions that the chairman was going to ask, and let me just in the interest of time proceed with his questions.

You state that: "At a request made by MBA VA task force, VA now supplies the full appraisal report, not just the certificate of reasonable value, to VA lenders." Since this occurrence have you experienced any change in underwriting procedures?

Mr. WYNN. To my knowledge, sir, the changes are not substantial. However, it does give us a basis to begin comparing the method of appraisal as compared to an FHA or a conventional loan. I think there will be some constructive suggestions and some constructive procedures come out of this over time, yes.

Mr. SUNDQUIST. Thank you, Mr. Wynn.

Anybody can answer this on the panel. You recommend that veteran applicants be restricted from having direct access to VA field offices regarding the status of their loan applications. Isn't this counterproductive to the VA's role of providing service to veterans?

Mr. WYNN. I will address that since it was in our testimony. We don't by any means think the veteran should be limited in any benefit that they are entitled to. What we are suggesting is that the emotion be taken out of the credit decision. Many times when you are face to face with a veteran the emotional aspect can cloud the judgment of the credit decision. Limited access is suggested to eliminate that emotional clouding.

That doesn't mean that we suggest that a veteran not be able to sit down and talk with a counselor about their financial problems. However, the credit underwriter should be taken out of the position where he is making decisions on emotions as opposed to the creditability of the potential borrower to repay the loan.

Mr. SUNDQUIST. In my experience in dealing with the Veterans' Administration, it is that they deal in very little emotion. Sometimes I wish they would deal with more emotion.

You think this is a serious problem?

Mr. WYNN. I don't consider it to be a serious problem. However, in some cases and in isolated instances it does become a problem.

Mr. SUNDQUIST. You recommend that VA lenders should make use of the procedure allowing VA to pay a partial claim in those

instances where someone can take over the property for less than is due. How often does this occur?

Mr. WYNN. It is infrequent, to my knowledge, sir.

Mr. SUNDQUIST. Pardon me?

Mr. WYNN. It is infrequent.

Mr. SUNDQUIST. Infrequent?

Mr. WYNN. It is done infrequently, to my knowledge.

Mr. SUNDQUIST. Thank you.

Do you have any VA mobile home loans in your portfolio?

Mr. WYNN. No, sir, I do not.

Mr. SUNDQUIST. Do you have an estimate in how many instances a loan application previously denied by a lender on an automatic approval basis is subsequently approved through another lender or through the VA?

Mr. WYNN. No, sir, I do not have an estimate on that.

Mr. SUNDQUIST. Mr. Wynn, are you satisfied with the overall status of the task force report?

Mr. WYNN. We would like to compliment VA in that during the process of the task force meetings they were very cooperative with us. They met with us. They worked with us. They have begun, without the final report, to implement many of the suggestions that we have had.

Because of the complexity of the report, we certainly want to be sure that the analysis of their response is given every consideration. We feel VA, as it has for many years in the past, will do everything they can to work with MBA to solve any differences that might still be between us from the recommendations that we made and their current responses to us.

Mr. SUNDQUIST. Thank you, Mr. Wynn.

Ms. Helfant, I appreciate your testimony. I am sorry I couldn't be here during that testimony.

I wanted to comment on your concern that the proposal may be detrimental to the VA revolving fund. That would be the last thing I would like to have occur. My interest is to put the VA revolving fund in a position where it doesn't need more money, where it is solvent, where we don't have to look for ways of charging the veterans more money on their loans.

What is your concern essentially there with my proposal?

Ms. HELFANT. I think our concern was adequately reflected by Mr. Wynn's statement. From our reading of the bill it can be interpreted that the discounts offered by virtue of the change of pricing factors in the marketplace would be geared to only a veteran who was in the market to look at VA foreclosures, rather than exposing the property generally to the broad-based market.

Mr. SUNDQUIST. I see.

Ms. HELFANT. Veterans and nonveterans.

Mr. SUNDQUIST. Are most realtors today familiar with VA foreclosed properties?

Ms. HELFANT. Mr. Sundquist, that is an interesting question. Our proposal for a model marketing plan which we worked with VA, on a task force to develop, was we felt that our practitioners were not giving adequate attention to VA foreclosures because they are somewhat cumbersome to deal with, and also since it has been in the last few years very much a buyers' market in most areas of the

country, real estate practitioners are going to show the property that can be moved most quickly, that can provide a prompt acceptance of an offer, and that gives various warranty incentives to the purchaser.

Mr. SUNDQUIST. I met with a group of realtors from west Tennessee and discussed H.R. 2801. And in the process as I talked to them and went in and looked at some of the property, it was my opinion from what is a very small sampling without question, that some of the property we have on the books at the VA is just not going to sell at that price and that we are kidding ourselves if we think we are going to get that much money out of it.

Do you have any comment on that, or any feel for that?

Ms. HELFANT. Having served this year as regional vice president representing the State of Tennessee and good realtors down in that end of the country, I would agree with that. I think that as we look at foreclosure properties it is like a car with mileage. A used car with mileage. If a home is not cared for it falls into disrepair and begins to depreciate; therefore, it may not be worth the original loan value.

Also, due to the various economic factors across the Nation a home could have appraised for $10,000 more in 1980 and because the plant has closed down and the town has literally closed down, the value may in fact, be falling.

Mr. SUNDQUIST. Thank you.

Mr. SHELBY. How has the VA received your task force marketing plan?

Ms. HELFANT. VA was part and parcel to the development of that plan and were very cooperative. I would like to commend the VA Director of the Loan Guaranty Program, Bob O'Toole, and his staff for giving us input along with your staff, Mr. Chairman, and it has been most helpful.

We are concerned about the problem. We feel the veterans need the program. We, as professional marketers of property, use the program. We want to make sure that it is as solvent as it can possibly be.

Mr. SHELBY. I had to go vote a minute ago. As you all can see, committees keep on going even when we have to vote. Therefore, I missed the basic thrust of your statement. It has been our feeling all along, however, that these properties have to be sold as soon as they can be marketed. The sooner the better. I have owned properties. As a lawyer I have been involved in real estate. The longer something remains vacant, wherever it is, it is going to deteriorate. You can say what you want to about it. I am sure that is the basic feeling of the realtors. You are professional marketers; and if your group can't market it, I don't know who can.

But homes have to have a realistic price don't they?

Ms. HELFANT. Yes, sir. And it must be easily accessible to the trade and the practitioners, also there must be a good response time from the agency, to the realtor and back to the buying public.

Mr. SHELBY. We appreciate you appearing here today, all of you.

Ms. HELFANT. Thank you, Mr. Chairman.

Mr. SHELBY. Excuse me. Counsel has one more observation.

Mr. WILSON. Mr. Wynn, is there any substantial differential between loans approved on an automatic basis and loans approved on a prior approval basis?

Mr. WYNN. In what regard, sir?

Mr. WILSON. In terms of foreclosures.

Mr. WYNN. There is a differential. There are more loans as a percentage of the ones that are approved—there are less loans that foreclose on an automatic basis as opposed to prior approval.

Mr. WILSON. Is it substantial?

Mr. WYNN. The term "substantial" would mean a large majority. I don't think it is a large majority. I think the ratio is somewhere like 2 to 1, perhaps.

Mr. WILSON. Thank you.

Mr. SHELBY. I thank the counsel.

Thank you again for appearing.

Mr. SHELBY. Our next panel is some of the service organizations: Mr. Rick Weidman, director of governmental affairs, Vietnam Veterans of America; Mr. Richard Schultz, Disabled American Veterans, associate national legislative director; Mr. Dennis Smurr, Paralyzed Veterans of America; Mr. Dennis Cullinan, Veterans of Foreign Wars; Mr. Philip Riggin, the American Legon; and Mr. Richard Johnson, Jr., director of legislative affairs, The Non Commissioned Officers of the United States.

Gentlemen, you are veterans of not only the service, but of this committee and many others. I appreciate your waiting patiently. You do however, have the benefit of the previous testimony. You are very knowledgeable in this area which affects your membership.

Your written testimony, as all of you know, will be submitted for the record in its totality without objection and made part thereof. If you could briefly sum up your testimony or your observations, it would help us.

Mr. Weidman, go ahead.

STATEMENTS OF RICK WEIDMAN, DIRECTOR OF GOVERNMENT AFFAIRS, VIETNAM VETERANS OF AMERICA, ACCOMPANIED BY DANIEL F. HAYES, ESQUIRE, SPECIAL COUNSEL; RICHARD F. SCHULTZ, ASSOCIATE NATIONAL LEGISLATIVE DIRECTOR, DISABLED AMERICAN VETERANS; R. DENNIS SMURR, ASSOCIATE LEGISLATIVE DIRECTOR, PARALYZED VETERANS OF AMERICA; DENNIS M. CULLINAN, SPECIAL ASSISTANT, NATIONAL LEGISLATIVE SERVICE, VETERANS OF FOREIGN WARS; E. PHILIP RIGGIN, DIRECTOR, NATIONAL LEGISLATIVE COMMISSION, THE AMERICAN LEGION; AND RICHARD W. JOHNSON, JR., DIRECTOR OF LEGISLATIVE AFFAIRS, THE NON COMMISSIONED OFFICERS OF THE USA

STATEMENT OF RICK WEIDMAN

Mr. WEIDMAN. Thank you, Mr. Chairman.

I would just like to thank you for allowing us, the Vietnam Veterans of America, to appear here this morning.

I wish to cover three basic things in our testimony here this morning. Number one is that we commend Mr. Sundquist for introducing H.R. 2801, the discounted loan program, and believe that it

would serve two needs well. One is to sell deteriorating housing which is losing value as a matter of sitting empty with no vested owner occupant; and secondly, lower the threshold for some vets to enter the housing market on a first-time basis. As you know, we have consistently held to the viewpoint that the housing program is a vital readjustment program for first-time homeowners, particularly impacting on Vietnam veterans at this time.

A second major point that we wanted to cover was the whole question of default. It strikes us at Vietnam Veterans of America that perhaps we need to look a bit further. Instead of looking at the algorithmic data, of which we have a surfeit, looking at numbers about what kind of mortgage was cut in the beginning, what kind of appraisal was given, et cetera. What we really haven't looked at is why are people going into default, what is going on with those individual veterans, and are there services available within the VA to help individuals through those rough times, whether it be employment services, whether it be counseling services for post-traumatic stress disorder, marital counseling, et cetera.

I think if you talk to our friends at the Mortgage Bankers Association and others you will find that we can certainly ameliorate the problem, number one, and, number two, get a firm handle on what we are talking about as to who really is going into default and why. Right now we are all thrown back on anecdotal evidence.

So we would urge you and this committee, Mr. Chairman, to consider calling for a GAO study and profile so we know exactly who we are talking about, and why, in fact, are people getting into the situation of going into default, and what can be done to correct it insofar as possible through administrative procedures and VA remedies.

The third and major body of our testimony this morning touches on a recap of our view of the manufactured home industry and our involvement in action outside of this committee. In January and February of 1985, we had numerous complaints and began to become aware that there might in fact be some widespread problems with packing invoices and other kinds of illegitimate activity in that area. As we looked into it further, we found that we had good cause to believe that it was in fact a real problem, that it was in fact nationwide, and that veterans were indeed being defrauded.

In early March of 1985, we decided to move to the concept of a class action suit. The basic problem, as outlined in our statement before, was that the Veterans' Administration and the Department of Justice were only moving where someone had gone into default. The vast majority of veterans who had purchased manufactured homes over the last 10 years have not gone into default. In fact, they have literally skimped on the baby's milk money in order to make the payments on time. As it stood at that point, these individuals have no redress and no recourse for the money that we believe, and the evidence is clear, that they overpaid for their manufactured homes. That they were overpaying on a monthly basis, and still to this day continue to overpay, is a source of outrage to VVA.

On April 24, we filed suit in U.S. District Court in Delaware against six major manufacturers and have moved to certify a class

on both sides of the suit, both for the Vietnam Veterans of America and for the individual veterans who may have been defrauded and to certify the manufacturers as a class on the other side.

We filed an amended brief on August 26, 1985, Mr. Chairman, and which we have provided you with a copy of that full amended brief.

Our basic intent here is twofold: Number one, to provide redress to the individual veterans, and secondly, and just as important, to help in any way possible bring about redress in the industry so that veterans in the future are not subject to the same illegitimate and illegal practices.

Thank you.

Mr. SHELBY. I want to tell you before we go on that I sincerely commend your organization for its activist position on behalf of all Vietnam veterans. I know you have been pursuing the overcharge in the manufactured housing, but you are also active in a lot of other areas. I thought I would take this moment to express my feelings on that.

Mr. WEIDMAN. Thank you, Mr. Chairman.

[The statement of Richard F. Weidman appears at p. 179.]

Mr. SHELBY. Mr. Schultz?

STATEMENT OF RICHARD F. SCHULTZ

Mr. SCHULTZ. Thank you, Mr. Chairman. On behalf of the Disabled American Veterans I would like to say how much we appreciate this opportunity to testify here today. I would like to discuss briefly some of the points that we have made in our statement.

In regards to H.R. 2801, while we have no official position on this bill, we do feel that if you are going to offer this program to creditworthy veterans who have not previously purchased a home you might want to also consider adding additional categories such as nonprofit groups, even the Veterans' Administration's Department of Medicine and Surgery could possibly use some of these homes to benefit veterans. We feel that in today's atmosphere, especially with the problems encountered with the aging veteran, that some of these homes could be put to good use in that area.

With regard to the home loan guarantee program, quite frankly we are concerned. We are concerned with the fraud, abuse, the schemes that have been identified by the Inspector General and by recent articles describing the widespread fraud in the foreclosures. We are also concerned with the appraisal practices. The fact that realtors have said that they prefer using VA fee appraisers because they give them less problems. We feel that this hurts the program, and we are concerned that these areas need to be further addressed.

We realize that the Veterans' Administration in dealing with veterans are trying to help veterans obtain a home. However, by approving home loan guarantees for veterans who cannot meet the payments and who subsequently go into default, we are not helping them at all. We are hurting them and the program.

So a lot needs to be done and it needs to be looked at as it has been addressed here today to determine the creditworthiness of veterans. We feel that the home loan guaranty program has been a

good program. It is evident by the millions of veterans that have benefited by it, the communities that have benefited by it, and we feel that action needs to be taken by the Veterans' Administration and by this committee to ensure that the Veterans' Administration continues to manage this program well and continues to see, or to assure that veterans and the Veterans' Administration are not being ripped off because of those individuals out there who would like to make a profit illegally at veterans and Veterans' Administration expense.

Thank you.

Mr. SUNDQUIST. [presiding] Thank you, sir.

[The statement of Richard F. Schultz appears at p. 190.]

Mr. SUNDQUIST. Mr. Dennis Smurr, of Paralyzed Veterans of America.

STATEMENT OF R. DENNIS SMURR

Mr. SMURR. Thank you, Mr. Chairman. On behalf of the members of Paralyzed Veterans of America, I appreciate this opportunity to testify here today.

Mr. Chairman, I think it is safe to say that the VA Home Loan Guaranty Program has been a benefit to the entire Nation. It has been a very successful housing program. But in the last several years, or more particularly the last 18 months, the home loan program has endured some of the most trying times of its 41-year existence. The figures indicate that in March of 1984 the VA had a record high inventory portfolio of over 22,000 properties valued at over $800 million and, as of last month, the VA Home Loan Guaranty Service has sold over 24,000 properties and generated over $1 million in revenue this fiscal year.

This, in part, can be attributed to the Nation's overall economic recovery, but PVA believes that credit must also go to Robert M. O'Toole, Director, and to the employees of the VA Home Loan Guaranty Service. Mr. O'Toole and his staff have instituted some very innovative management practices which have helped reduce the inventory portfolio to its current level of approximately 18,000 units. This reduction is especially noteworthy in light of the fact that new foreclosures continue at a very high rate. We feel confident the VA Home Loan Guaranty Program can and will do well in meeting the rigorous demands that continue to menace the Nation's housing market.

In our review of H.R. 2801, PVA sees merit to this bill, but we do not think such legislation is needed at this time. The VA already has the administrative discretion to discount the sale price of properties in its inventory portfolio, and it exercises this authority on a case-by-case basis. We feel this approach is more prudent and economically advantageous than that which is proposed in H.R. 2801.

We also view H.R. 2801's stipulation limiting such a discount sale to a veteran who has not previously purchased a dwelling unit as being discriminatory. To be fair H.R. 2801 must provide purchase options to veterans who may have lost a previously guaranteed home due to divorce, unemployment or disability. The Loan Guaranty Service might do well to incorporate an H.R. 2801-type program on a regional basis as individual inventories dictate. Such a

program could be activated by a triggering mechanism at VA central office on the basis of a predetermined inventory threshold, one that reflects current real estate marketing trends and the economic conditions existing in a given region in the United States. The affected VA regional office could then make available to interested veterans a listing of the discounted properties.

H.R. 2801 may need to be instituted sometime in the future, but until such conditions dictate, PVA would rather have the VA Loan Guaranty Service retain its discretionary authority in handling its foreclosed property portfolio.

As to the issue of the fraud which has been perpetuated against veterans and the VA by the manufactured home industry, PVA applauds the efforts of the VA Inspector General and his staff in bringing to justice those manufacturers who have violated the law. We also want to compliment the Atlanta, Georgia, VA regional office home loan staff for uncovering this practice. The Inspector General's report indicates that nearly half the Nation's major mobile home manufacturers have offered to plead guilty to charges of padding sales invoices and defrauding the Government, this is indicative of two facts: the fradulent practice is widespread, and maybe the invoicing policy of the VA for the purchase of manufactured homes needs to be reviewed and possibly revised. If this be the case, then PVA would hope that an industrywide organization such as the Manufactured Housing Institute or the National Manufactured Housing Finance Association would be willing to work with the appropriate Veterans' Administration officials to develop a better invoicing method.

More importantly, the manufactured housing industry needs to initiate an aggressive campaign of policing its own member manufacturers to rid itself of present questionable practices, and to reestablish itself not only with veterans and the VA, but with the American public, in general.

Mr. Chairman, that concludes my testimony. Thank you.

Mr. SUNDQUIST. Thank you very much for your testimony.

[The statement of R. Dennis Smurr appears at p. 202.]

Mr. SUNDQUIST. Mr. Cullinan, special assistant to national legislative service, Veterans of Foreign Wars. Thank you for being here.

STATEMENT OF DENNIS M. CULLINAN

Mr. CULLINAN. Thank you, Mr. Chairman and members of the subcommittee. On behalf of the membership of the Veterans of Foreign Wars, I thank you for this opportunity to present our views on the fraud perpetrated on veterans by certain unscrupulous profiteers in and associated with the manufactured housing industry. Additionally, H.R. 2801, introduced by Mr. Sundquist, will also be addressed.

The VA home loan program is one of the most successful and beneficial VA programs servicing veterans, and a key element is the availability of guaranteed loans for the purchase of manufactured homes. Particularly today, in light of the rapidly escalating cost of housing, a manufactured home is often all a veteran can afford. When competent and reputable individuals are responsible for their production and sale, they may be affordable, nicely fur-

nished dwellings. Unfortunately, swindlers in this industry have been defrauding unsuspecting veterans, predominantly lower income veterans, for years and in many instances turned the American dream of homeownership into a nightmare of debt and foreclosed home loans.

Investigators contend such illegal schemes as packing or kickback fraud and charging for nonexistent items have gouged more than $100 million from buyers, the Federal Government and conventional lenders. VA officials suspect that manufacturers padded the invoices for 80 percent or more of the 295,000 homes shipped last year.

The Veterans of Foreign Wars are absolutely appalled by these activities and adamant that those responsible be prosecuted to the full extent of the law and that proper compensation and restitution be made to all the veterans who have been so victimized and to the VA itself.

We are also of the opinion that the steps to prevent such abuse are long overdue and should be initiated immediately. We believe the first step toward eliminating fraud, or such fraud, is by financing manufactured homes the same as are site-built homes, based on individual appraisals rather than on manufacturers' invoices. Further, we would like to see closer monitoring of the manufactured home industry with an eye toward at least providing veterans with a listing of reputable manufacturers and dealers.

It would also be well advised, we feel, to provide veterans who are about to purchase either a manufactured or a site-built home with a VA counselor or adviser to advise him as to the pitfalls and problems and obligations of homeownership. The pamphlets and other written materials currently available are admirable, but are not sufficient in themselves given the complexity of such a transaction and coupled with the attendant excitement of making what is for most people the largest purchase of a lifetime.

Also of discussion at this time is legislation introduced by a distinguished member of the subcommittee, the Honorable Don Sundquist. This bill, H.R. 2801, would establish a discounted home sales program by the VA for veterans for buying their first homes. Inasmuch as this would benefit veterans and the VA home loan program by reducing its holding time of certain real properties and consequently cost, it enjoys strong VFW support. We highly commend you, sir, for having devised and introduced this innovative and constructive measure.

Mr. Chairman, once again thank you for holding this hearing and for requesting our participation. This concludes my remarks.

Mr. SHELBY. Thank you very much for your testimony.

[The statement of Dennis M. Cullinan appears at p. 209.]

Mr. SUNDQUIST. Next, an old friend of mine, Mr. Riggin of the American Legion.

STATEMENT OF E. PHILIP RIGGIN

Mr. RIGGIN. Thank you, Mr. Chairman. We recognize the subcommittee's time constraints this morning and we will certainly keep our verbal statement very brief.

As always, the American Legion is pleased to have the opportunity to present its views on the VA home loan program for your consideration.

The topics of today's hearings are certainly timely in that recent revelations of fraud by the manufactured housing industry should be carefully examined, and where fraud has been committed the guilty should be stiffly penalized.

Also, the general subject of VA property management practices is very important, obviously, noting the size of the VA's inventory of foreclosed properties at this time. Anything that can be done to expedite the sales of these properties will certainly bolster the loan guaranty revolving fund and the direct loan revolving fund. In that regard, H.R. 2801 is an important contribution to the growing dialogue on how VA should dispose of its inventory.

Mr. Chairman, obviously the record of this morning's hearing is completely full of the manufactured housing problem. We will not comment on that verbally, but we will comment on your legislation. The last time this subcommittee held oversight hearings on the VA home loan program VA testified, in part, on the progress it was making in the sale of its inventory of foreclosed properties. At that time the agency stated that it was devoting greater resources to the marketing of these properties and was offering special sales of these properties in different locations around the country. These activities were said at that time to be helping VA in disposing of such properties. The American Legion is encouraged by these developments and sincerely hopes that VA has been successful and will continue to be successful.

Your legislation introduced on June 18 is intended to augment the tools already available to VA in the marketing of foreclosed properties. The American Legion principally views this bill as a good faith step in the right direction which would properly recognize the economic constraints of first-time homebuyers, veterans who are first-time homebuyers, and, of course, the secondary focus seems to be directed toward inventory properties which are hard to sell. Both of these are legitimate considerations but we think that certain protections should be guaranteed when this legislation moves forward.

First, it should be made clear that nothing in H.R. 2801 is intended to restrict current VA procedures designed to quickly sell inventoried properties. And I don't believe that you have suggested anything that would stop that current practice, or impede that current practice.

Secondly, the quality of properties sold under provisions of this measure must be assured. Presumably, if a foreclosed property is being and has been aggressively marketed by VA and remains on the inventory for an extended period, the property is likely to be defective in its structural integrity or from a habitability standpoint. Since the veteran purchaser under H.R. 2801 would use the property as a principal residence, VA, of course, should assure that the property is livable condition—and that has already been discussed this morning as well.

While the discounts in the pending measure are substantial, there may be economically depressed localities around the country in which greater discounts would be necessary to stimulate first-

time homebuyer veteran interest. We, therefore, recommendation that this subcommittee consider granting certain authority, if necessary, for greater discount rate flexibility. Hopefully such increased flexibility would encourage sales before properties are rendered virtually unmarketable because of physical deterioration.

Mr. Chairman, that concludes our statement, and again we thank you for the opportunity to present testimony here.

Mr. SUNDQUIST. Thank you, Mr. Riggin for being here today and your excellent testimony.

[The statement of E. Philip Riggin appears at p. 213.]

Mr. SUNDQUIST. You get the privilege of going last, Mr. Johnson.

STATEMENT OF RICHARD W. JOHNSON, JR.

Mr. JOHNSON. I am not sure whether that is enviable position or not, Mr. Chairman.

Mr. SUNDQUIST. We appreciate you being here.

Mr. JOHNSON. Thank you very much. Let me try and summarize what everybody else has said.

First, on behalf of the Association, we extend our appreciation to the committee for the amount of attention that the committee has given the loan guaranty program this year. It is, indeed, a somewhat troubled program, but in many regards the troubles of the program are transitory.

As we have said in previous testimony, we view the loan guaranty program to be very sound, one of the most sound in its structure in Government today; and we reminded the committee at the same time that this was never intended to be a cost-free program. Indeed, at its inception the loans to veterans were reduced by an arbitrary amount made as a grant by the Government. Over the years the program has cost less than $80 per veteran as an operating expense of Government.

How then did we get to the shortage that we have today? Looking at it in 20/20 hindsight we can see two reasons. First there was a major change in the late 1970's with the management of the VA's loan portfolio and that came at the same time as a major recession in the United States which led to high foreclosure rates. As a result, the VA lost the income from managing its portfolio, which had paid for the operation of the program through some 25 years of its operation while acquiring large numbers of properties. It took a long time to get where the program is today, to create the debt the program has, and it will take a long-term solution to get the program out of debt.

As an Association, NCOA believes that that recovery will come from some forebearance on the part of this committee, some additional appropriation on the part of this committee, but a restoration of management practice in the VA loan portfolio. Go back to managing properties, quit the fire sale mentality of unloading properties as quickly as possible, and begin to manage those properties again for a profit. Begin to manage that portfolio again for the profit, so that the program will once again become self-supporting, self-sustaining.

With regard to the Inspector General's investigation into fraud in the manufactured housing industry, NCOA extends its commen-

dation to the VA—to Mr. Hincken, Mr. Sato, and the other people that are involved in that investigation. However, we would ask the Veterans' Administration to go one step further in the voluntary agreements they are reaching with manufactured home sellers and manufactured home manufacturers. We would very much like to see the Veterans' Administration seek reimbursement to all veterans who are defrauded in this scheme as opposed to just those veterans who have defaulted on their home. And in the absence of gaining restitution for all veterans involved in the program, we would like to see the VA go ahead with full prosecution of the manufactured homebuilders and manufactured home manufacturers involved.

That concludes my remarks, Mr. Chairman. I would be happy to answer any questions you may have.

Mr. SUNDQUIST. Thank you very much, Mr. Johnson.

I thought you summarized the situation very well, and that is an advantage of going last.

Mr. JOHNSON. It is, indeed.

[The statement of Richard W. Johnson, Jr., appears at p. 218.]

Mr. SUNDQUIST. Do I understand that in your last comment on manufactured homes, you are saying the investigation should include those who presently own as well as those who lost?

Mr. JOHNSON. Yes, sir. Those people were defrauded on the same basis that everybody else was. They are the victim of a false certification, and in many cases their loss will be several thousand dollars spread over the life of the loan they got.

Mr. SUNDQUIST. Absolutely. I will pass that message on to the chairman. I agree with you on that—yes, sir.

Mr. WEIDMAN. If I may comment, Mr. Chairman. The determination, rightly or wrongly, but the way in which the Department of Justice and the Inspector General's Office were interpreting the law is that they felt they could not go after the manufactured home folks, various parts of the industry that had perpetuated the fraud if, in fact, the guaranty had never been invoked, meaning they would pursue a case only if a default, had occurred. This is why Vietnam Veterans of America filed the class action suit, specifically to address the need of the overwhelming majority of folks who had not defaulted, and who were denying their family lots of things in order to make those payments on time. It is those 95 percent of the folks that our suit is trying to get refunds to, essentially.

Mr. SUNDQUIST. The class action suit will cover those individuals?

Mr. WEIDMAN. That is specifically who it is, sir.

Mr. JOHNSON. If I may, Mr. Shelby, first off, I would like to extend commendations to our colleagues at VVA for having entered in that suit. However, I think what is underlying here is the Veterans' Administration has a fiduciary responsibility in that they were defrauded through the false certification and they have an obligation to protect the veteran. I agree with Mr. Weidman. I agree with the determination of the Department of Justice in that they could only prosecute and receive criminal fines from the individuals that are involved.

However, the Veterans' Administration in negotiating settlements with these companies can include all veterans in those nego-

tiated settlements. And what I am suggesting is, if all veterans involved are not included in those negotiated settlements, then prosecution for the fraud should go ahead.

Mr. SUNDQUIST. Well, Mr. Johnson, I agree with you. On the other hand, the Inspector General can proceed with urging from this committee to move into those areas as well. I can only speak for myself, but I would urge the VA to do that.

Mr. Riggin, I want to go back. By the last in/first out method of accounting here, I just got a couple of questions; not many. I think that with some 18,000 homes that we are holding, and I heard the VA testify a few minutes ago that they hope to get that down to 16,000 shortly. To me, we ought to be thinking in bigger terms than that.

Mr. RIGGIN. I think so, too, Mr. Chairman. Obviously, if you are working to get down to 16,000 in the foreseeable future, many of those 16,000 that remain have surely been on the list for a long, long time.

Mr. SUNDQUIST. 30 percent I think is the figure.

Mr. RIGGIN. And anything that can be done in a constructive fashion to rid VA of its inventory properties is a step in the right direction, regardless of previous comments regarding market value or anything else. Market value certainly is a major consideration, but it can't be the only consideration.

Mr. SUNDQUIST. Thank you. And thank you for your testimony.

Mr. Cullinan, obviously with the manufactured homes we don't want to do anything here that will destroy the program. I think that was the point you were making. It is a good program and we want to make sure that the program be maintained, but we must get rid of and stop the unscrupulous people from participating.

How widespread do you think the problem is?

Mr. CULLINAN. Well, we heard from the Inspector General earlier that it is extensive and from the materials we have at our disposal it is nationwide. Our figures show that 80 percent or more of the homes shipped last year were affected by either packing or charging for nonexistent items. I am not quite certain of the proportion. I believe it is predominantly the packing fraud. So it is very extensive, indeed, and many, many veterans have been hurt by this fraud. And that is why we, too, call for restitution and compensation of all veterans who have purchased manufactured homes.

Mr. SUNDQUIST. I think we ought to make it clear that the committee in no way is impugning the industry. I think it is a good industry basically. We think that it serves a good purpose, as you outlined, and our purpose is to strengthen the industry.

Mr. CULLINAN. Yes, sir. And to eliminate the fraud and abuse that exist within it. It is not the entire industry apparently, but just certain individuals within it.

Mr. SUNDQUIST. Absolutely. Thank you for your testimony.

Mr. CULLINAN. Thank you, sir.

Mr. SUNDQUIST. Mr. Smurr, in your testimony you are saying that the VA already has discretion to do this. What they don't have, though, is the mandate that if anybody is going to get a break it ought to be veterans, and that is the point I think that you ought to consider. If we are going to give a break on these houses

to anybody, we ought to give them to the veterans first. That is what the program is for.

And in terms of your comments that a veteran who may have lost his home because of divorce, unemployment or disability, I have no problem including those people in the piece of legislation. I think that what I proposed was a concept that recognizes what I think is a fact, that we have too many houses in inventory, and it is going to cause the program some problems. We ought to get rid of some of those that have been there a long time. We shouldn't put more money into them and let them set. Let us let a veteran do it, or get into that home at a rate that he or she can afford and could not perhaps get into otherwise.

You have any comment on that?

Mr. SMURR. Mr. Sundquist, we wholeheartedly agree with the fact that the veteran should be the one to benefit from any kind of a discount program, and we appreciate your introduction of that legislation. We appreciate also the fact of your being willing to include the veteran that lost a home due to the three factors mentioned.

We view that what the VA is facing is large inventory portfolios on a regional basis. And if we don't include people that are displaced because of employment, divorce, or other factors in your legislation, we had concern with that. But we do appreciate your comment.

Mr. SUNDQUIST. Thank you for your testimony.

Mr. Weidman, one quick question. I think we need to find out more, as you outlined, about the veteran defaults and the foreclosures. Is there any other way we could do it other than GAO? Is that the only vehicle you would propose that we could use?

Mr. WEIDMAN. Well, there may be another way to do it. By mandating VA to contract out a study of the profile. And to some degree what it has to be is someone who knows the broad range of services, not just within the Veterans' Administration, but within the veterans' service network, if you will, Mr. Chairman, so that if you find out, for instance, Dennis' point about divorces, a very high number of divorces. I mean, our divorce rate, let us be blunt about it, among Vietnam vets is double our cohort group, and in many cases PTSD is involved. And the question is, obviously, and the experience is that is a common reason for people defaulting and going into foreclosure on their home, because of income being reduced in two-income-earner families.

If you recognize that early on and if the proper mechanisms were set up within the Veterans' Administration to where in fact the individual would come in when they first started to get into trouble, and the folks in the loan section, guaranty section, know to refer them to the Readjustment Counseling Service, to Behavioral Sciences, and to others—Family Services, for instance—within the Veterans' Administration and link the individual up with the service, we could solve the problem, as opposed to essentially playing banker inside the VA.

Now, this is not by any means intended to be a rap on Mr. O'Toole and his folks. I think they have made some strides in that direction and they are starting to, the latest jargon is interface

with other parts of DVB. But we believe that there is a heck of a lot further that they can go in that direction.

Mr. SUNDQUIST. Thank you, and I agree with you. And I would like you to discuss on a personal basis and not as a member of this committee, the GAO estimate, if you would, with us.

We have a vote. I just have one more question.

Mr. Schultz, the suggestion of DAV in terms of using these houses in some other areas, I have no problem with it if it makes sense and will help the veteran. And I appreciate your testimony.

I would like to thank Chairman Montgomery for his leadership on this committee and our chairman of this committee, who had to leave, for holding the hearings today, and Ms. Royce for setting up the hearing, and all of you for being here. We appreciate it.

The subcommittee is adjourned.

[Whereupon, at 11:55 a.m., the subcommittee was adjourned.]

APPENDIX

STATEMENT OF RAYMOND J. VOGEL
CHIEF BENEFITS DIRECTOR
VETERANS ADMINISTRATION
BEFORE THE
SUBCOMMITTEE ON HOUSING
AND MEMORIAL AFFAIRS
COMMITTEE ON VETERANS' AFFAIRS
HOUSE OF REPRESENTATIVES
SEPTEMBER 12, 1985

Mr. Chairman and Members of the Subcommittee:

It is a pleasure to appear before you this morning to discuss the operation of the Veterans Administration's housing program. I have with me today Robert M. O'Toole, Director, Loan Guaranty Service and James P. Kane, Assistant General Counsel.

Mr. Chairman, your invitation to appear before the subcommittee requested we discuss a number of specific areas, including the future financing of the loan guaranty program. In recent years the Loan Guaranty Revolving Fund, which provides moneys for all loan guaranty operations except administrative expenses, has been substantially depleted. A supplemental appropriation of $100 million (Pub. L. No. 98-396) and an appropriation transfer to the fund of $160 million were both needed in Fiscal Year 1984 in order to enable the program to meet its obligations in that year. Additional funding was provided by Pub. L. No. 98-473 which appropriated $306.6 million for Fiscal Year 1985.

Current budget projections indicate an end-of-year unobligated balance of approximately $230 million, therefore, requiring no supplemental appropriation for the remainder of FY 1985.

We are currently making every effort to maximize sales (both cash sales of properties and vendee loan sales) and thus reduce appropriations to the Loan Guaranty Revolving Fund. Through July of this fiscal year, we have received $254 million in cash proceeds from the sale of VA-acquired property (including down payments on vendee loans), an amount more than triple the $81 million collected during FY 1984. The FY 1985 sale of 16,293 vendee loans generated $681 million, which includes $9 million in premiums over the face amount of the loans, due to recent declines in interest rates.

While revenue generated from these asset sales helps to reduce our appropriation requirements, it does not fully offset expenditures associated with the continued high level of defaults and foreclosures. The Revolving Fund is still facing financial difficulties. We are hopeful, however, that a continued reduction in our inventory of acquired property will lessen the program's future funding requirements.

Mr. Chairman, you also requested that we discuss current Property Management practices. Although we continue to experience high levels of foreclosures completed during FY 1985 (an average of 2,666 per month), we have made considerable progress in our

property sales volume and expect this upward trend to continue in FY 1986. Property sales through July total 23,643, 22 percent higher than the comparable period in FY 1984. In fact, in just ten months we have already exceeded the total number of properties sold in FY 1984 (22,235). In May 1985, our field stations sold 3,035 properties, the highest monthly sales since September 1966. We expect that FY 1985 property sales will exceed 28,000 and will generate $1.2 billion in revenue to the Loan Guaranty Revolving Fund.

In March 1984, we reached our highest number of properties in title: 22,316. By the end of FY 1984, we had reduced that figure to 21,895, and, as of the end of July 1985, we had achieved a reduction to 18,783, with an additional 12,973 properties pending acquisition by VA due to the continuing high foreclosure level.

In addition to reducing our property inventory over 16 percent during FY 1985 in the face of high foreclosure levels, we implemented two provisions of the Deficit Reduction Act of 1984: collection of a one percent funding fee and sale of a minimum of 25 percent of VA properties for cash. Through July, we have collected over $97 million in funding fees required by the Act, $7 million of which was collected on vendee loans, and 26.7 percent of our sales this year have been for cash.

Several program changes that were implemented in FY 1984 and early in FY 1985 to promote sales have proven successful, and continued emphasis on these changes has helped us to accelerate the downward

trend in our inventory during FY 1985. These programs include: considering below list offers on properties that have been on the market for more than 6 months; paying sales commission bonuses up to $500 on older and lower priced hard-to-sell properties; allowing a 10 percent discount for those purchasers who pay cash; paying reasonable discount points where outside financing is obtained by the purchaser, and using real estate auctions to sell properties in certain areas of the country. The auction method is only used in those areas where sales efforts have been unsuccessful using ordinary sales practices. In FY 1985, we held auctions in Detroit, Houston, Peoria and Cedar Rapids. In these four auctions we sold 696 properties for over $11.5 million. Auctions are scheduled for the remainder of CY 1985 in Portland, Phoenix, and Los Angeles.

The continuing improvement in our Property Management sales activity is reflected in the following:

	Properties Sold
FY 1981	10,671
FY 1982	10,857
FY 1983	18,634
FY 1984	22,235
FY 1985	28,000 (projected)

Mr. Chairman, another item you wished to discuss was H.R. 2801. This bill would authorize the Administrator to sell, at a discount, properties acquired by VA to certain veterans.

Under H.R. 2801, if VA has been unable to sell a property for at least 3 months, it could be sold at a discount to a veteran who has never previously owned a home and who has VA home loan entitlement.. The discount could be up to 30 percent, depending upon how long the property has been in VA's inventory.

Once VA acquires a property, we undertake to sell it in order to recoup at least a portion of our loss on the guaranty. Our primary goal in selling these properties is to receive the best possible price and terms in order to maximize the Government's recovery of its investment.

Although any member of the public may purchase properties from VA, purchase offers submitted by veterans receive a limited preference over similar offers from nonveterans. Factors such as all cash offer, amount of offer, and degree of credit risk do, however, take precedence over the buyer's veteran status.

The sale of acquired properties has never been intended as a benefit for veterans. It is solely a salvage operation to defray the costs to the taxpayers of operating the VA home loan program. VA opposes turning this business operation into a benefits program.

Under current law we have the authority, and, in fact, do offer certain properties for sale at a discount. We believe, however, that market forces should be the primary factor determining the

sale price of our acquired properties, and that any discount deemed desirable to dispose of a property should be available to any qualified buyer.

VA estimates that enactment of H.R. 2801 would result in a net reduction of sales income of approximately $115 million in FY 1986, and a 5 year net reduction of $474.5 million.

Accordingly, Mr. Chairman, while VA opposes enactment of H.R. 2801 as not being timely, we will keep it under consideration should our other attempts to sell properties not prove fruitful.

A final item requested for discussion was the recent frauds perpetrated by the manufactured housing industry and the actions VA will take in response. The specifics of the manufactured home invoice padding scheme are covered in the testimony of the VA Inspector General's Office. In the early stages of the investigation, at the request of the Office of Inspector General, it was agreed that no changes in procedures would be made. We are now, after consultation with the Inspector General, considering changes in procedure to assure that such fraudulent practices will not occur in the future. One proposal under consideration is to revise the current dealer invoice certification to require full disclosure of all rebates or discounts received by the manufactured home dealer from the manufacturer, including volume purchase discounts.

Mr. Chairman, I am sure the committee would also be interested in knowing of current actions in the area of underwriting. VA will continue to strive to ensure that only financially capable, credit-worthy veterans receive VA home loans. Realizing the effects of continued high levels of defaults and foreclosures, coupled with the disinflation in home prices, we issued a policy statement in May of this year to all VA Regional Offices. The statement reemphasized to our field stations the importance of quality underwriting, with particular attention devoted to avoiding the following unacceptable practices:

- Accepting at face value, without details and documentation a borrower's explanation for a bad credit history.

- Approving loans based on an emotional appeal from the borrower, sales agent, or seller.

- Reopening and reversing a previous decision to reject a loan without new and compelling information.

- Approving "marginal" applications without adequate review and discussion among a group of underwriters where possible.

- Failing to require a borrower who is weak in one area, such as cash assets, to demonstrate strength in other areas such as income and credit history.

- Unjustifiable reliance upon short-term or irregular income to qualify a borrower for a loan.

Our offices were also instructed to review and update the figures used to estimate family support requirements and maintenance and utility expenses. These figures are now made available to interested lenders. Loan Guaranty seminars were recently held which included a discussion of credit underwriting. We are also developing a computerized capability to better identify lenders with a higher than acceptable record of defaulted loans.

Mr. Chairman, this concludes my statement. I will be pleased to respond to any questions that you or Members of the Subcommittee may have.

Number of Properties on Hand
As of August 31, 1985

State	Number of Months						
	<6	6-11	12-17	18-23	>24	Subject to Redemption	Total
Alabama	32	8	4	2	2	137	185
Alaska	30	8	2	0	0	0	40
Arizona	162	85	50	6	16	0	319
Arkansas	73	17	5	5	6	0	106
California	655	877	412	164	83	0	2,191
Colorado	315	131	30	8	3	0	487
Connecticut	19	12	10	1	4	0	46
Delaware	3	3	0	0	0	0	6
District of Columbia	17	9	8	3	3	0	40
[illegible]da	310	112	21	4	1	0	448
[illegible]ia	220	142	75	16	4	0	457
Hawaii	7	1	0	0	0	0	8
Idaho	58	32	14	4	7	0	115
Illinois	584	386	203	94	108	273	1,648
Indiana	277	307	149	104	142	0	979
Iowa	135	119	84	69	122	209	738
Kansas	120	70	41	18	23	88	360
Kentucky	68	30	9	3	0	3	113
Louisiana	88	76	59	19	12	0	254
Maine	15	6	4	3	1	0	29
Maryland	96	31	33	9	4	0	173
Massachusetts	2	0	1	0	1	0	4
Michigan	242	216	116	94	87	251	1,006
Minnesota	140	72	28	9	18	120	387
Mississippi	45	22	6	1	4	0	78
Missouri	73	51	26	12	8	0	170
Montana	31	30	21	9	8	1	100
Nebraska	40	14	16	14	6	0	90
Nevada	128	181	72	20	13	0	414
New Hampshire	4	2	0	0	0	0	6
New Jersey	173	117	50	13	31	0	384
New Mexico	24	8	2	1	1	2	38
New York	62	37	22	9	14	0	144
North Carolina	155	34	17	4	10	0	220
North Dakota	19	9	5	1	2	7	43
Ohio	608	529	201	97	60	0	1,495
Oklahoma	193	94	66	11	13	0	377
Oregon	37	44	23	24	23	1	152

State	Number of Months <6	6-11	12-17	18-23	≥24	Subject to Redemption	Total
Pennsylvania	219	144	36	25	44	0	468
Puerto Rico	37	14	11	7	11	0	80
Rhode Island	0	0	0	0	0	0	0
South Carolina	91	40	22	9	1	0	163
South Dakota	9	3	9	4	10	10	45
Tennessee	125	57	19	3	5	0	209
Texas	763	809	363	192	150	0	2,277
Utah	52	26	5	2	0	0	85
Vermont	2	1	0	0	0	1	4
Virginia	146	49	10	3	1	0	209
Washington	267	143	40	25	17	0	492
West Virginia	31	26	5	6	7	0	75
Wisconsin	129	126	100	44	46	0	445
Wyoming	61	45	13	6	4	1	130
U.S. Total	7,192	5,405	2,518	1,177	1,136	1,104	18,532
8/31/84 U.S. Total	7,882	6,472	3,312	1,517	1,453	1,004	21,640]

OPENING STATEMENT OF ROBERT A. HINCKEN

VETERANS ADMINISTRATION

ASSISTANT INSPECTOR GENERAL FOR INVESTIGATIONS

BEFORE THE HOUSE VETERANS' AFFAIRS COMMITTEE

SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS

SEPTEMBER 12, 1985

Mr. Chairman and Members of the Committee, I am pleased to be here today to discuss our recent investigations regarding various types of frauds perpetrated against the VA Guaranteed Home Loan Program. As we are presently involved in sensitive ongoing criminal inquiries in this area, I will limit my comments to general statements on some of the types of fraudulent schemes we are encountering.

Our recent investigations have uncovered three types of fraudulent schemes that have a direct impact on the integrity of the Veteran Administration's Loan Guaranty Program and which are victimizing veterans participating in the program. Two of the schemes involve the VA's Mobile Home Loan Guaranty Program, and a third scheme involves "site built" homes purchased under VA loan guarantees.

The VA's Mobile Home Loan Guaranty Program is administered under the provisions of Section 1819 of Title 38, United States Code and the 4200 Series of VA Regulations. Under these provisions, the VA guarantees 50% or $20,000 of the mobile home loan amount, whichever is less. Ninety percent of the guarantees are by automatic lenders who have the authority to grant loans without prior VA approval. During fiscal years 1982 through 1984, the VA guaranteed about 37,000 mobile homes for loans totaling over $769 million. During this same period, about 5,000 loans went into default and were terminated causing the VA to pay over $36 million in default claims.

The amount of the VA guarantee is based on the manufacturer's invoice to the mobile home dealer. The VA requires the manufacturer to certify in writing that the manufacturer's invoice price reflects the dealer's cost at the point of manufacture, and except for discounts based solely on volume purchases, that the invoice price does not include other discounts, bonuses, refunds, rebates, prizes or anything of value which would inure to the benefit of the dealer.

In July 1984, we initiated a nationwide investigation involving 52 mobile home manufacturers regarding a practice known in the mobile home industry as "invoice padding" or "packing" to determine if illegal rebates were occurring in the VA's Mobile Home Loan Guaranty Program. Our investigations have revealed that "invoice padding" is extensive throughout the mobile home industry, and that some manufacturers include unit rebates in invoice prices in spite of the fact that they certified that they had not done so. In addition, we have determined that veterans were often charged for accessories that were not provided and that these items were included on the invoices submitted to the VA and included in the amount guaranteed. As a result of these practices, the VA may have overpaid an estimated $3 million on defaulted mobile home loans.

As a result of our investigation to date, four manufacturers have entered negotiated guilty pleas to criminal charges and signed settlement agreements to repay the VA for its losses. Investigations involving five additional manufacturers are in the final negotiation stages.

Another fraudulent scheme that has recently come to our attention involves the resale of repossessed mobile homes. This scheme is perpetrated by individuals who are commissioned by lending

institutions to resell the repossessed units. After the lending institutions repossess VA mobile homes that have gone into default, the units are appraised by a VA fee basis appraiser. The repossessing agent then sells the mobile homes at or near the appraised value and submits false documents showing that the homes sold for considerably less than the appraised value or the true sales price. The VA is then asked to pay the difference between the fraudulent sales price and the veteran's indebtedness, up to the amount of the VA loan guarantee.

A third type of fraud we are presently investigating involves various companies who, through fraud and misrepresentation, are acquiring title to conventionally built homes which were delinquent or in default. Our office has received a number of investigative referrals concerning alleged violations of the equity skimming Section of Title 12, United States Code. The violations involve approximately 17 companies, more than 80 veterans, and represent potential losses to the VA in excess of $1 million.

Under an equity skimming scheme, the offending company seeks out a veteran who is in financial difficulty and who has placed his home on the market "for sale by owner". The company contacts the veteran and offers to purchase the home under certain stipulations. They offer a 2nd trust deed as payment, payable in three to twelve months, and also promise to pay the monthly mortgage payments until they are able to sell the home. The veteran is required to immediately vacate the property so the company can rent the house and realize some income; income the veteran is led to believe will be applied to the mortgage payments.

When the veteran attempts to collect from the company at the end of the promissory note period, he is either stalled or ignored and eventually discovers that the company has no intention of paying the note as agreed. He also discovers that the company pocketed the rental proceeds, has made no mortgage payments on the property, and intends to let the property go into foreclosure.

Various types of equity skimming schemes have been uncovered and are under planned or active investigation. As it appears that equity skimming activities may be widespread, the Office of Inspector General has recently published an Alert Bulletin designed to alert veterans about the equity skimming fraud and to provide them with information on how to avoid becoming victims. The Bulletin has also been distributed to mortgage companies that make loans to veterans with a request from the VA Administrator for the companies to work with the VA in protecting the homes and equity of veterans.

Mr. Chairman, this concludes my statement.

STATEMENT OF
THE MANUFACTURED HOUSING INSTITUTE
BY
JERRY C. CONNORS, PRESIDENT
BEFORE
THE COMMITTEE ON VETERANS AFFAIRS
SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS

HEARINGS ON
THE VETERANS ADMINISTRATION HOME LOAN
GUARANTY PROGRAM
SEPTEMBER 12, 1985

MANUFACTURED HOUSING INSTITUTE
JERRY C. CONNORS, PRESIDENT
1745 JEFFERSON DAVIS HIGHWAY
ARLINGTON, VIRGINIA 22202

(703) 979-6620

INTRODUCTION

The Manufactured Housing Institute

The Manufactured Housing Institute (MHI) is a national trade association representing builders of manufactured homes. There are about 170 companies producing homes in over 400 factories across the United States. About one-third of those companies are members of MHI. These manufacturers, however, account for about two-thirds of all manufactured homes produced annually in the U.S. MHI members also include 225 companies that supply a wide variety of goods and services to producers and consumers of manufactured housing.

The Manufactured Housing Industry

The advantages of mass production spawned the development of factory-built housing over 50 years ago. Today there are several forms of factory-built homes including modular, panelized, and manufactured. Our remarks today concern themselves with the form of factory-built housing known as manufactured homes. Manufactured homes are delivered from the factory in one or more sections. They are completely assembled and require only minimal labor to make them ready for occupancy once delivered to a home site. Manufactured homes are built to federal standards prescribed by Congress in the National Manufactured Home Construction and Safety Standards Act of 1974 (P.L. 93-383). These standards were developed and implemented by the Department of Housing and Urban Development (HUD) in June 1976. As a result of HUD's involvement, these standards are commonly known as the HUD code, and manufactured homes are referred to as HUD code homes. Since that time, HUD has maintained its surveillance of the manufactured housing industry primarily through its agent, the National Conference of States on Building Codes and Standards. Innovative technology, improved aesthetics, and a federal construction code that ensures consistent health and safety standards throughout the U.S. have all played a significant role in making manufactured housing an important part of the permanent housing stock in America.

From January 1, 1980 through June 30, 1985, a little more than halfway through the decade of the 1980's, manufactured home builders produced 1,433,083 homes, accounting for 15.6 percent of the 9,178,400 total privately-owned housing construction started during that 5 1/2-year period (See Table 1). The 1983 Annual Housing Survey (H-150-83), published by the U.S. Department of Commerce, Bureau of the Census, indicates that there were 88,637,000 full-time occupied housing units at the end of 1983, including manufactured homes. Full-time occupied manufactured homes accounted for 3,999,000 housing units or 4.5 percent of the total occupied housing units in the U.S. at the end of 1983. (See Table 2 for a state by state comparison of manufactured housing producers, suppliers, retailers, and occupants based on estimates by MHI.)

The Veterans Administration Manufactured Home Loan Program

The Veterans Administration (VA) was first authorized to guarantee loans on manufactured homes by of the Veterans' Housing Act of 1970 (P.L. 91-506). The 1970 Act provided for a termination of the program on July 1, 1975 to give Congress time to evaluate this new program. The program became permanent with the passage of the Veterans Housing Act of 1974 (P.L. 93-569), and Congress affirmed its belief that the VA Manufactured Home Loan Program was beneficial and provided a good source of housing to veterans. The program has provided 96,564 veterans the opportunity to own their own home during the 15-year period from 1970 to July, 1985. For this reason, we believe that the program is an important and valuable part of the overall benefits provided to veterans through the various activities carried out by the VA. Manufactured home loans guaranteed by the VA are eligible for pooling into Government National Mortgage Association (Ginnie Mae) mortgage backed securities. As such, the program also provides an important conduit to loan funds available through institutional investors and others who buy Ginnie Mae securities. Access to investors through secondary markets has become an increasingly important source of funds for housing finance in the 1980's. And, Ginnie Mae, at this time, is the only organized secondary market source for manufactured home personal property loans.

The Purpose of These Remarks

We very much appreciate the opportunity to appear before the subcommittee today to discuss the industry's views of the VA manufactured home loan program and to focus on alleged improprieties in invoicing practices in the manufactured housing industry. As the subcommittee is aware, the program has come under scrutiny by the VA's Inspector General. The Inspector General has alleged that some manufactured home builders have made false certifications to the VA regarding discounts or rebates offered to retailers of manufactured homes. There have been a number of news articles on the Inspector General's investigation. These articles have contained some inaccurate and unfair characterizations of the alleged violations. Without a clear explanation, we fear that these unfortunate and erroneous news accounts have created the impression that the veteran is not being benefited through the program. We do not believe this to be the case, in fact. The purpose of our remarks is to describe the practices we understand the Inspector General to be examining, to describe the market forces that have created and sustained these practices, to describe steps already taken by members of MHI and others in the manufactured housing industry to deal with manufactured home financing generally, and to recommend steps to be taken on a cooperative basis by the VA and the manufactured housing industry to deal specifically with the concerns of the VA and this subcommittee.

The subcommittee is no doubt aware that in addition to the investigation being conducted by the VA Inspector General, the Vietnam Veterans of America have filed a class action law suit against a number of manufacturers and others. In light of these as yet unresolved legal issues, we should emphasize that these remarks represent a composite

view of what we see as the issues. They in no way represent the plans or practices of any individual manufacturer or other members of the manufactured housing industry. The examples used are for illustrative purposes only, and should not be construed to represent any actual transactions, either past or present, in the manufactured housing industry.

FINANCING MANUFACTURED HOUSING

Overview

Before proceding to our more detailed examination of manufactured home financing under the VA program, two critical points must be made. First, the retail price which a buyer pays for a home, whether it be purchased with a VA guaranteed loan or a conventional loan, is determined through negotiations between buyer and seller, with the buyer having the opportunity to shop with multiple sellers. The VA acknowledged and accepted this fact in establishing the program and therefore never intended to establish or control the retail price of a manufactured home. Instead, the VA controlled only the maximum loan amount. Any difference between the sales price and the maximum loan amount was to be paid by the veteran through a downpayment.

The administrator of the Veterans Administration explained this in a letter dated July 20, 1970 to the chairman of the House Committee on Veterans Affairs.

> "Since the retail purchase price of a specific model of a new mobile home may vary from dealer to dealer, as in the case of new automobiles, it is not practical to base a downpayment requirement on the retail price or reasonable value, if by reasonable value it is intended to mean retail price. It is for this reason we proposed to adopt a limitation in the form of a maximum loan amount at a figure which will result in approximately a 10-percent downpayment. However, it could be less or more, depending on the price the veteran agrees to pay."

Second, the manufactured housing industry is highly competitive and innovative and has used a variety of rebate and incentive programs to maintain and build market share regardless of the mode of financing, whether VA or conventional. Such rebate and incentive programs are common to all highly competitive industries. In the discussion which follows, we illustrate one way in which a legitimate marketing incentive plan might have been used. Of course, benefits provided under such a program might have been utilized in many alternate ways. Again, it is important to note that these examples are hypothetical, and not examples of programs actually in use by any particular member of the manufactured housing industry.

The Wholesale Invoice

The method of computing loan amounts for financing most manufactured homes is significantly and fundamentally different from the real estate financing methods prevalent in other home finance transactions. Unlike other forms of single-family housing, manufactured home financing is not based on an appraisal when purchased new. Rather, a lending institution bases the amount of retail financing on the wholesale price or invoice price of the home. The invoice price is the amount the seller of the home, the retailer, pays to the producer of the home, the manufacturer. The vast majority of manufactured homes are delivered with furniture, drapes, carpets, and appliances included. The cost of such things as air conditioning, installation of the home at a site, transportation of the home from the manufacturing facility to the retailer and other items are usually eligible for financing as well.

A simplified example of a wholesale invoice for a manufactured home might typically contain the following information:

Table 3

Base Price (including furniture, drapes, carpeting, and appliances)	$20,000
Optional Air Conditioner	1,200
Transportation (Freight) Charges	500
Wholesale Price to Retailer	$21,700

In this example, the retailer would pay $21,700 for the home. Obviously, he will sell the home for a higher price to cover his operating costs, including his profit margin. The amount the retailer will seek to mark up the home will depend on his operating costs, competition from other retailers and competition from other forms of similarly priced housing in his market area. The actual retail price that the home is sold for, of course, will be the result of negotiations between the retailer and the buyer. Once established this becomes the legitimate price of the home, regardless of the method or amount of financing or downpayment.

To illustrate how a retail price for a manufactured home might be determined, an example of what an abbreviated income statement might look like for the sale of a manufactured home is presented in Table 4. The relationships in Table 4 between the invoice price (or cost of sales), sales price, gross profit and net profit are based on a survey of retailers conducted by Robert Morris Associates, a nationally known organization that compiles financial information for use by lenders and financial analysts. The survey did not include every retailer in the United States, but it does provide a reasonable benchmark for analysis.

Table 4

Sales (retail price of home)	$27,820	100%
Less Cost of Sales (wholesale price of home)	21,700	78
Gross Profit	6,120	22
Less Operating, Administrative and other Costs	5,560	20
Net Profit	$ 560	2%

Having arrived at a sales price he would like to obtain for the home, the next step is to find a willing buyer or, conversely, for a buyer to find a retailer who is offering a home for sale with the amenities that the buyer needs and at a price the buyer is willing to pay. The VA estimates that there are about 7,000 retailers in the U.S. Most of them carry the homes of several different manufacturers. This high number of retail establishments indicates that there is rigorous competition among retailers and, therefore, ample opportunity for consumers to shop for homes with the amenities and sales price that fits their needs. In most cases the buyer must secure a loan for the major portion of the cost of the home. Obviously, the higher the amount of the loan proceeds, the lower the downpayment requirement will be for the buyer. For low and moderate income buyers, a low initial cash investment is very often the key ingredient to making the transaction work. One reason that veterans have initially been attracted to the VA loan guaranty program for manufactured housing is the perception that it is a low or no downpayment program. Although, in fact, a low downpayment may not be possible, as we will demonstrate later.

When the VA program for site-built housing was created in 1944, one of the objectives was to provide home financing for veterans with lower downpayments than were available through conventional loan programs. By the time the manufactured home program was created in 1970, the 26-year trend of low or no downpayment loans had been established. Even though the manufactured home program was not necessarily intended to mirror the downpayment characteristics of the site-built program, historically veterans have come to believe that VA loans require a low or no downpayment. Hence, there is resistence to downpayments. In many cases, it is impossible for veterans to come up with much, if any downpayment. In order to compete with other forms of housing available to the veteran (lower cost site-built housing, condominiums and co-ops), the manufactured home retailer may choose to offer financing on terms and conditions that are similar to or better than those available from the competition, or he may choose to compete in other ways. He might, for example, utilize one of the rebate or incentive plans offered by manufacturers to effectively reduce the downpayment.

In the example from Table 4 the maximum loan that the regulations permit the VA to guarantee is computed as follows:

Table 5

Base price of Home	$20,000
Add Cost of Air conditioner	1,200
	21,200
Time Percent Advance	120%
Add Cost of Freight	500
Maximum Loan Amount	$25,940

The loan proceeds, then, are limited to $25,940 in this transaction.

The retailer cannot sell the home without a downpayment under the conditions illustrated in Table 4. Selling the home for only the loan proceeds of $25,940 will result in a net loss to the retailer.

Table 6

Sales (retail price of homes)	$25,940	100%
Less Cost of Sales (wholesale price of homes)	21,700	84
Gross Profit	4,240	16
Less Operating, Administrative, and other Costs	5,560	21
Net Loss	($1,320)	(5%)

At a minimum, an additional $1,320 in cash must be raised from loan proceeds or a downpayment or both.

Raising the sales price to $27,260 will yield a break-even point. But, it will require the veteran to put up the $1,320 as a downpayment, since the loan proceeds are limited to $25,940 based on the manufacturer's invoice price and VA regulations governing maximum financeable amount. If the manufacturer had in place, however, an incentive program , the cost of which is reflected in the wholesale invoice, but on a net basis, after receipt of the benefit, the retailers wholesale cost was unchanged, then a downpayment reduction could be achieved as illustrated below. Such a benefit program could either be a volume incentive program, in which the costs are spread over a particular product line, or it could be reflected in the cost of the particular home in question. If it was the former, then it could be legitimately financed in accordance with the VA program requirements. If the latter, then it could not, as explained more fully later.

Assume that the value to the retailer of the incentive program is $1,000 for the home in our illustration. Further, assume for the purpose of simplicity, that the manufacturer's incremental cost for this home and the retailer is $1,000. The actual cost to a manufacturer under a volume incentive plan could, of course, vary depending on the level of participation by the retailer. The manufacturer's invoice becomes:

Table 7

Base Price (including furniture, drapes, carpeting and retailer discount)	$21,000
Optional Air Conditioner	1,200
Transportation (Freight) Charges	500
Wholesale Price to Retailer	$22,700

The retailer's sales price and net profit remain the same:

Table 8

Sales		$27,820	100%
Less Cost of Sales			
Invoice Price	$22,700		
Discount	- 1,000	21,700	78
Gross Profit		6,120	22
Less Operating, Administrative, and other Costs		5,560	20
		$ 560	2%

The maximum loan amount, however has increased $1,200 from $25,940 to $27,140.

Table 9

Base Price of Home	$21,000
Add Cost of Air Conditioner	1,200
	22,200
Times Percent Advance	120%
	26,640
Add Cost of Freight	500
Maximum Loan Amount	$27,140

Using the original sales price of $27,820 as computed in Table 4, the required downpayment has been lowered by $1,200 from $1,880 (6.8%) to $680 (2.4%). The result of the discount has been a larger loan and lower downpayment, not an increase in the price of the home to the veteran. In the face of the substantial competition from other retailers, as well as from other forms of similarly priced housing, there is no reason to believe that any given retailer possesses sufficient market share to allow him to control prices.

The VA's Policy on Discounts and the Inspector General's Investigation

As a practical matter, company marketing practices are established to meet the competition. In the case of manufactured home builders, that competition is substantial. Some 170 manufacturers competed for sales of 294,993 homes to retailers in 1984. There is a low concentration of market share among manufacturers on both a national and regional level. Table 10 shows comparative market shares of the largest manufacturers over the last five years. There is a high level of substitutability in the manufactured home product. Retailers in any particular market area will be served by a number of manufacturers offering homes of similar design, amenities and cost. Manufactured home builder executives know that there is very little product loyalty among retailers. They are price, rather than brand, conscious. It is in this context that the VA certification requirements must be considered.

The VA circular 26-79-26 requires manufacturers to certify their invoices for homes to be financed with loans guaranteed by the VA as follows:

> "The undersigned certifies that the manufacturer's invoice price shown on this invoice reflects the dealer's cost at point of manufacture, exclusive of any and all freight or transportation charges and, excepting discount based solely on volume purchase, net of any and all discounts, bonuses, refunds, rebates, prizes or anything of value which will inure to the benefit of the dealer at the time of purchase or at any future date."

The circular goes on to explain that:

> "VA's definition of a volume rebate is 'an established company marketing practice offered to all dealers on an equal basis for volume purchases over a stated period of time.' Rebates on single units or small volume purchases are not considered eligible rebates."

Under the circular, therefore, if a manufacturer established a volume incentive program, the cost of that program to the manufacturer could be included in the base price of the home on the invoice, and fully financeable under the VA program without the need for separate

disclosure. If, on the other hand, the manufacturer established a single unit or small volume purchase discount or rebate program, the cost of such a rebate would have to be subtracted from the wholesale invoice prior to computing the maximum amount financeable. Thus the cost of this latter category of programs is not financeable under the VA program.

The VA's definition of volume rebates and small volume purchases appeared to manufacturers to provide substantial latitude to design programs that would volume spur sales. Manufacturers used the discretion provided to create programs of varying types and benefit levels, and may in certain instances have wandered into the gray areas under the circular. Now unfortunately, the Inspector General, with the benefit of hindsight, is claiming that certain programs are not eligible as volume rebates and that manufacturers making this certification have, in some cases, offered rebates that the Inspector General considers ineligible as volume incentive plans.

A determination of whether a rebate or discount was eilgible or ineligible has been, or will be, made for past transactions which the Inspector General is investigating. On a going forward basis, however, we think that there are steps that can be taken through cooperative efforts of VA and members of the manufactured housing industry that will prevent future violations or misunderstandings of VA policy.

SOLUTIONS TO THE PROBLEM

The Program Works

We believe that the VA Home Loan Guaranty Program for manufactured housing has worked well over its 15 year history and continues to benefit veterans. We also believe that the VA program staff has worked diligently and effectively in administering the program to assure that veterans received the housing benefits that the Congress has authorized. We mentioned earlier that almost 97,000 veterans have used the program to realize the benefits of home ownership. Without the program, many of these veterans may well have had to forgo those benefits. The problems associated with invoicing practices in the manufactured housing industry are not insurmountable. We would respectfully suggest that the problem can be effectively addressed through the cooperative efforts of the VA and the manufactured housing industry, without the need for further legislation.

The Truth in Invoicing Practices Statement

MHI has recently developed a Truth in Invoicing Practices Statement (statement). It was approved by the MHI Board of Directors to be recommended for general use in the industry. Because it deals with invoicing practices, and therefore could raise some antitrust questions, we have submitted and are now waiting for an answer to a request for a business review letter from the Antitrust Division of the Department of Justice. We have asked the Department of Justice to act as expeditiously as possible.

The statement focuses on the disclosure of invoicing practices used by manufacturers. It is intended to give lenders and government agencies, like the VA, the information they require to make an informed decision about a manufactured home loan. It attempts to avoid the gray areas that we believe are present in the VA certification requirements by offering a number of guidelines related to volume purchase discounts. We believe that it is these gray areas that have led to most of the alleged improper rebates being examined by the Inspector General. It requires a certification by the manufacturer that the information he is giving on the invoice is true and accurate to the best of his knowledge and belief. It is not intended to dictate to manufacturers the kinds of marketing plans they should use or to cast all marketing plans in a single mold. It is intended to provide a framework within which manufacturers may provide any and all information that lenders and others require to make an informed business decision about whether they wish to make the loan, and if so, the dollar amount of the loan. If successful, the statement will provide lenders and others with a level of comfort that the information they receive is adequate and accurate.

VA and Industry Discussions

In the past, when the industry has encountered difficulty in using or understanding the program, we have found the VA program staff to be cooperative and helpful. In this situation, however, discussions have been prevented by a gag order put in effect by the Inspector General becuase of the ongoing investigation. We understand that the Inspector General is now willing to rescind that order. We believe, therefore, that it is now time to begin a series of meetings with the VA to discuss the invoicing issue and solutions to problems that have arisen in the program.

Recommendations

As stated earlier, we think that the VA manufactured home loan guaranty program has played a significant role in providing affordable housing to veterans. As such, we would strongly advocate its continuation. We respectfully submit that there is no need for further legislative action in this area. The problems that we have discussed today can be addressed through clarifications and revisions of the VA program requirements.

First, there needs to be an immediate clarification of the certification requirements with respect to discounts and rebates. Any past activity which may have been inappropriate in the VA program has been, or will be settled as the Inspector General's investigation continues. On a going forward basis, however, the industry needs clear guidance to avoid any misunderstanding of what is and what is not acceptable under the VA progam requirements. Second, the program regulations need to be examined, through the rulemaking process of proposed regulations. Through this process, the program can be

modified from being only perceived as a low downpayment program to being actually a low downpayment program. Such things as the maximum amount financed, allowances for set-up, transportation and other costs incidental to a manufactured home purchase transaction need to be examined in this context. A much more detailed approach to invoicing practices, such as the Truth in Invoicing Practices Statement developed by MHI, needs to be examined and implemented. Third, the concept of moving away from invoice-based financing to appraisal-based financing needs to be examined. We hasten to add here, however, that this needs to be done carefully and deliberately. Currently there is no system to appraise new manufactured homes. Any appraisal system developed must be on a voluntary and trial basis until such time as there is conclusive evidence that such a system works effectively, efficiently, and on a timely basis.

CONCLUSION

As we said earlier, we think the program has worked well over its 15-year history, to the benefit of almost 97,000 veterans. The invoicing problems that have arisen are being dealt with through the Inspector General's investigation. We think further strides in finding a permanent solution to this problem can be made through the cooperative efforts of industry and the VA. MHI stands ready to adopt and recommend for industry use a voluntary procedure for disclosures and certifications about information in invoices. We are anxious to work with the VA to get this problem behind us so that the VA and the industry, working together, may provide affordable housing to America's veterans.

Table 1

	Manufactured Homes Produced	Privately-Owned Housing Units Started	Total Housing Production	Manufactured Housing as a % of Total Housing Production
		(Thousands of Units)		
1980	221.6	1,292.2	1,513.8	14.6%
1981	240.9	1,084.2	1,325.1	18.2
1982	238.8	1,062.2	1,301.0	18.4
1983	295.1	1,703.0	1,998.1	14.8
1984	295.0	1,749.5	2,044.5	14.4
1985 (Jan.-June)	141.7	854.2	995.9	14.2
TOTAL	1,433.1	7,745.3	9,178.4	15.6%

Table 2

MANUFACTURED HOUSING INSTITUTE
GOVERNMENT RELATIONS DEPARTMENT
SUMMARY OF MANUFACTURED HOUSING BY STATES

States	# of M.H. Facilities	# of M.H. Suppliers	# of M.H. Retailers	# of M.H. Occupants	Total # of M.H.	# of Homes Shipped in 1984	# of Homes Produced in 1984	Estimated Annual $ to the Economy
CAN.	10	7						7,945,700
AK	0	6	23	43,117	19,599	286	*	13,554,400
AL	30	44	135	409,978	186,354	11,318	23,623	97,685,500
AR	6	26	145	194,217	86,898	6,295	2,854	82,728,800
AZ	8	28	134	344,650	156,659	6,694	5,937	79,457,100
CA	32	107	1,000	999,937	454,517	10,425	12,683	532,362,400
CO	4	26	125	197,330	85,776	1,634	1,075	72,446,200
CT	0	7	44	31,022	14,101	321	0	23,837,100
DC	0	0	1	858	390	0	0	467,400
DE	0	1	53	68,347	31,067	2,287	0	25,239,300
FL	43	76	1,475	1,200,000	600,000	30,990	23,160	745,027,000
GA	32	73	310	618,635	281,198	17,879	48,660	193,968,800
HI	0	5	0	920	418	0	0	2,337,000
IA	2	10	154	131,307	59,685	944	*	77,587,500
ID	11	18	84	117,587	53,449	1,747	5,033	52,815,600
IL	0	24	373	341,873	155,397	3,357	*	185,555,700
IN	45	85	355	351,377	159,717	5,120	24,370	226,686,400
KS	14	44	137	176,565	80,257	2,325	5,390	91,141,900

States	# of M.H. Facilities	# of M.H. Suppliers	# of M.H. Retailers	# of M.H. Occupants	Total # of M.H.	# of Homes Shipped in 1984[c]	# of Homes Produced in 1984	Estimated Annual $ to the Economy
KY	1	7	167	292,217	132,826	5,750	*	81,794,000
LA	6	30	184	398,257	181,026	11,432	2,939	102,826,800
MA	1	11	74	45,533	20,697	671	0	40,195,900
MD	1	13	82	87,454	39,752	1,290	*	44,869,900
ME	3	6	69	91,898	41,772	1,301	*	36,456,800
MI	5	26	369	455,851	207,205	6,346	*	186,957,800
MN	9	19	154	204,751	93,069	1,944	2,755	85,065,800
MO	5	17	248	302,650	137,568	5,579	1,501	126,196,500
MS	6	19	109	252,276	114,671	6,404	8,761	62,630,900
MT	2	10	51	115,434	52,470	1,251	*	29,445,900
NC	27	55	580	705,665	320,757	24,637	28,197	309,415,200
ND	2	5	46	40,132	31,878	621	0	24,771,900
NE	5	10	66	59,145	26,884	717	3,383	37,859,000
NH	2	5	73	65,533	29,788	1,087	*	37,391,600
NJ	1	12	113	67,071	30,487	564	0	58,891,700
NM	1	2	93	173,947	79,067	4,780	0	44,869,900
NV	1	1	53	117,378	53,354	1,532	0	25,706,000
NY	3	34	392	377,313	171,506	5,993	*	200,512,300
OH	4	38	450	306,066	203,051	5,444	3,504	229,958,100
OK	2	14	240	155,995	126,108	6,411	896	119,653,000

States	# of M.H. Facilities	# of M.H. Suppliers	# of M.H. Retailers	# of M.H. Occupants	Total # of M.H.	# of Homes Shipped in 1984	# of Homes Produced in 1984	Estimated Annual $ to the Economy
OR	13	37	115	197,617	125,093	2,548	6,818	77,120,100
PA	22	66	457	359,158	234,555	5,857	14,396	254,730,000
PR	0	1	1					935,800
RI	0	1	18	5,658	4,377	127	0	8,880,500
SC	1	14	342	335,744	189,712	15,074	*	166,859,900
SD	0	5	37	47,898	33,258	823	*	19,630,600
TN	10	34	135	238,103	148,960	6,834	12,011	83,663,600
TX	61	127	1,104	1,019,480	463,400	37,462	41,627	603,873,800
UT	3	6	47	51,048	35,401	1,025	*	26,174,100
VA	6	26	163	210,012	138,439	6,515	5,065	91,141,900
VT	1	2	26	30,065	19,308	562	*	13,554,400
WA	5	26	161	300,000	165,000	6,014	1,314	89,739,800
WI	10	30	166	122,179	92,863	394	3,206	96,283,300
WV	0	5	131	168,269	84,975	3,150	0	63,565,700
WY	0	6	30	40,207	31,336	563	*	16,826,200
Total	456	1,307	11,094	12,667,724	6,286,095	294,993	295,013	6,009,292,500

*These states have less than three manufacturers, and for proprietary reasons figures are aggregated.

Sources:
1. Merchandiser Magazine, 1985 (includes non Manufactured Housing Institute (MHI) members, plants, and corporate facilities).
2. Manufactured Housing Institute (includes MHI members only or approximately 80 percent of nation wide total.)
3. Merchandiser Magazine.
4. U.S. Bureau of Census; National Conference of States on Building Codes and Standards.
5. U.S. Bureau of Census; National Conference of States on Building Codes and Standards.
6. National Conference of States on Building Codes and Standards.
7. National Conference of States on Building Codes and Standards.
8. Manufactured Housing Institute (based on annual industry contribution to the GNP of $6 billion).

Table 10

MARKET SHARE AND RANK IN PERCENT OF HOMES PRODUCED

NAME OF COMPANY	1984 HOMES BUILT	1984 RANK	1984 MKT SHARE	1983 HOMES BUILT	1983 RANK	1983 MKT SHARE	1982 HOMES BUILT	1982 RANK	1982 MKT SHARE	1981 HOMES BUILT	1981 RANK	1981 MKT SHARE	1980 HOMES BUILT	1980 RANK	1980 MKT SHARE
Fleetwood Enterprises	39579	1	13.4%	37746	1	12.8%	22296	1	9.3%	15417	2	6.4%	12891	4	5.8%
Champion Home Builders	19689	2	6.7	21715	2	7.4	19373	2	8.1	18571	1	7.7	15193	2	6.9
Skyline Corporation	15879	3	5.4	16118	3	5.5	13644	4	5.7	14907	3	6.2	16390	1	7.4
Redman Homes	15791	4	5.4	15406	4	5.2	11838	5	5.0	13022	5	5.4	11848	6	5.4
The Commodore Corp.	12023	5	4.1	14588	5	4.9	14961	3	6.3	14298	4	5.9	13068	3	5.9
Palm Harbor Homes	10509	6	3.6	4016	17	1.4	NA	NA	NA	NA	NA	NA	NA	NA	NA
Fairmont Homes	10112	7	3.4	9779	9	3.3	8331	9	3.5	8049	9	3.3	6124	9	2.8
Guerdon Industries	10000	8	3.4	11749	6	4.0	10860	6	4.5	11735	6	4.9	12179	5	5.5
Scott Housing Systems	9706	9	3.3	5152	14	1.7	NA	NA	NA	NA	NA	NA	NA	NA	NA
Liberty Homes	9489	10	3.2	10565	8	3.6	10199	7	4.3	10770	7	4.5	10369	7	4.7
Tidwell Industries	9443	11	3.2	10949	7	3.7	7297	11	3.1	6086	13	2.5	4289	15	1.9
Brigadier Homes, Inc.[1]	7907	12	2.7	8819	10	3.0	8655	8	3.6	8364	8	3.5	8075	8	3.7
Flintstone Industries	7784	13	2.6	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Kaufman & Broad	7294	14	2.5	7363	11	2.5	4797	14	2.0	6134	12	2.6	5305	11	2.4
Schult Homes Corp.	6125	15	2.1	6981	12	2.4	5733	12	2.4	6172	11	2.6	5803	10	2.6
River Oaks Industries	5881	16	2.0	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Zimmer Corporation	5794	17	2.0	6321	13	2.1	5241	13	2.2	5611	14	2.3	4736	13	2.1
Conner Homes Corp.	5721	18	1.9	4964	15	1.7	2843	20	1.2	2824	20	1.2	NA	NA	NA
Horton Homes, Inc.	5271	19	1.8	4857	16	1.6	4049	17	1.7	3120	18	1.3	3367	18	1.5
Clayton Homes	5170	20	1.8	3975	18	1.3	3160	19	1.3	NA	NA	NA	NA	NA	NA
Oakwood Homes Corp.	4291	21	1.5	3724	20	1.3	3269	18	1.4	2768	21	1.2	3005	20	1.4
DeRose Industries	3183	22	1.1	3263	21	1.1	2786	21	1.2	NA	NA	NA	NA	NA	NA
Wick Building Systems	3169	23	1.1	3770	19	1.3	4777	15	2.0	5533	15	2.3	5169	12	2.3
Fuqua Homes, Inc.	2804	24	1.0	2612	25	0.9	2081	25	0.9	2652	22	1.1	2539	23	1.1
Vintage Enterprises	2700	25	1.0	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Melody Homes Mfg.	NA	NA	NA	3138	22	1.1	4071	16	1.7	3938	17	1.6	3370	17	1.5
Moduline Int'l.	NA	NA	NA	3118	23	1.1	2762	22	1.2	2985	19	1.2	3146	19	1.4
Golden West Homes	NA	NA	NA	2619	24	0.9	NA	NA	NA	2632	23	1.1	2732	21	1.2
All American of Ashburn	NA	NA	NA	NA	NA	NA	7330	10	3.1	7414	10	3.1	4200	16	1.9
Shelter Resources[2]	NA	NA	NA	NA	NA	NA	2300	23	1.0	4118	16	1.7	4454	14	2.0
Homes of Merit	NA	NA	NA	NA	NA	NA	2197	24	0.9	2469	25	1.0	2682	22	1.2
Peachtree Homes[3]	NA	NA	NA	NA	NA	NA	NA	NA	NA	2567	24	1.1	2240	25	1.0
Nobility Homes	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	2393	24	1.1

Notes: NA = data not available
1. Brigadier is also reported in some years as U. S. Home Manufactured Housing.
2. Shelter Resources was purchased, in part, by Tidwell Industries.
3. Peachtree Homes was purchased by Kaufman & Broad.

Source: Mobile/Manufactured Home Merchandiser Magazine.

BEFORE

THE COMMITTEE ON VETERAN'S AFFAIRS

SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS

HEARINGS ON

H.R. 2801 AND THE VETERANS ADMINISTRATION
HOME LOAN GUARANTY PROGRAM

SEPTEMBER 12, 1985

STATEMENT OF

THE NATIONAL MANUFACTURED HOUSING FEDERATION

BY

WILLIAM D. BEVILLE, CHAIRMAN
AND
WILL EHRLE, PRESIDENT
TEXAS MANUFACTURED HOUSING ASSOCIATION

NATIONAL MANUFACTURED HOUSING FEDERATION
1015 15th Street, N.W., #1240
Washington, D. C. 20005

BEFORE THE
SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS
COMMITTEE ON VETERAN'S AFFAIRS
U.S. HOUSE OF REPRESENTATIVES
SEPTEMBER 12, 1985

STATEMENT OF THE
NATIONAL MANUFACTURED HOUSING FEDERATION

BY WILL EHRLE and
WILLIAM D. BEVILLE

INTRODUCTION

Hon. Richard Shelby, Chairman, Subcommittee on Housing and Memorial Affairs; Members of the Subcommittee: My name is Will Ehrle, and I am President and General Counsel of the Texas Manufactured Housing Association. Joining me today is Mr. William D. Beville, who is Chairman of the National Manufactured Housing Federation and also a retailer of manufactured housing in Fort Worth, Texas.

We submit this joint statement today on behalf of the National Manufactured Housing Federation ("NMHF"). NMHF is a non-profit trade association chartered in the District of Columbia whose membership is composed of 44 state manufactured housing trade associations. The National Manufactured Housing Federation represents through the various member state associations approximately 30,000 business firms in the United States. The membership of some of the state trade associations includes all segments of the industry, such as: retailers, manufacturers, manufactured home community and park owners and

operators, lenders and financial institutions, suppliers of goods and services, etc. Other state trade associations only represent a particular segment of the industry such as retailers or manufactured home rental communities. NMHF estimates that there are between 8,000 and 10,000 retail sellers of manufactured homes in the United States. We appear today on behalf of these retailers of manufactured housing.

PURPOSE OF HEARING

Mr. Chairman, as we understand it, and as indicated in your letter, there are several purposes for this hearing; however, your letter of invitation to NMHF to present testimony today stated that the "Subcommittee will focus on recent frauds perpetrated by the manufactured housing industry and others."

Our testimony will thus be focused on this particular query.

Mr. Chairman, we are reminded of some of the lessons which we learned in school relating to logic, to false premises, and to quantum leaps of invalid deductions. Some of the recent media accounts of the Veterans Administration Inspector General investigation of invoicing practices in the manufactured housing industry -- along with your letter -- we believe have fallen into the trap of false logic and invalid deductions. An example:

FACT:	XYZ Company illegally pads its invoices --
FACT:	XYZ Company is a manufacturer of manufactured housing --
THEREFORE:	Manufacturers of manufactured housing illegally pad invoices --

Mr. Chairman, this simply is not true. The manufactured housing industry is not engaged in fraudulent invoicing practices nor is it perpetrating any frauds. Unfortunately, a few companies have been involved in questionable business practices relating to retailer rebates and bonus programs.

Consciencious and dedicated Members of Congress -- representatives of the media -- or any other group certainly do not condone wrongdoing by any member of their group -- nor do they want the "few" to be characterized as the "whole". Neither do we in the manufactured housing industry. We deplore any fraudulent practices on the part of a very few.

VETERANS ADMINISTRATION COMMENDED MH PROGRAM BENEFITS VETERANS

The National Manufactured Housing Federation commends the Veterans Administration for a job well done over the fourteen years since the first manufactured home loan was processed and the VA guaranty issued. NMHF also commends the Inspector General's office for the current investigation which has focused attention on certain invoicing practices of a very few members of the industry. As mentioned hereinabove, we want any fraudulent practices on the part of the few eliminated.

However, Mr. Chairman and Members of the Subcommittee, we really get upset when the manufactured housing industry, as a whole, is indicted through false logic and invalid deductions.

The Veterans Administration manufactured home loan guaranty

program, authorized by Congress in 1970 and implemented in 1971, has been an extremely beneficial program for this nation's veterans. Since the first home loan guaranty in mid-1971 through July, 1985, the VA has guaranteed 96,564 manufactured home loans with an aggregate loan amount of $1,684,130,131. The average loan guaranty amount is $17,441. Thus, almost 100,000 deserving veterans have been able to realize the dream of home ownership through the purchase of code-built, durable, affordable manufactured homes. But for this program, these veterans and their families might otherwise never have been able to afford a home of their own. NMHF urges that this outstanding program be continued.

Perhaps, Mr. Chairman, you and other members of the Subcommittee have wondered why two Texans were before you today speaking on behalf of the National Manufactured Housing Federation. The answer to that is that the Veterans Administration manufactured housing loan guaranty program has been a popular one among Texas veterans. Since the inception of this program through July of 1985, 17,559 veterans have purchased homes in Texas under this program. This accounts for 18.18% of all the VA guaranteed manufactured home loans in the country during the life of the program. Thus, almost 1/5 of the total number of homes included in the program have been purchased by veterans living in Texas. Obviously, this is an important program for the manufactured housing industry as well as for our

veterans in the State of Texas.

In fact, the program has been very popular throughout the sunbelt and particularly in the oil and gas producing states of Louisiana, Oklahoma and Texas. Through July, 1985, since the inception of this program 22,302 manufactured homes have been purchased in these three states by veterans utilizing this home loan guaranty program -- 23% of the total for the nation.

The economy in these three states is not good. The oil "glut" and cheap imports have taken a heavy toll in all the energy producing states, but particularly in these three. Many thousands of workers have been laid off, and drilling and new discovery programs have almost become non-existent. Many veterans have worked in the oil patch, and many of these have purchased manufactured homes through the VA loan guaranty program. Now, repossessions abound. Times are not good, and loan defaults are numerous. However, this does <u>not</u> mean that this program is faulty or has not been administered properly. The program is sound, and the VA has done an excellent job. The economy is the guilty party; the economy is the "perpetrator" of the repossession problems.

Since the inception of the VA manufactured home loan guaranty program through July 31, 1985 there have been a total of 4104 repossessions in the states of Louisiana, Oklahoma, and Texas. We believe that a large number of these have occurred during the past three years -- during the economic slump in these

three states.

But this situation is not limited to manufactured homes. The Mortgage Bankers Association of America reported that a record of 6.2% of residential mortgages were 30 days or more past due in the fourth quarter of 1984.

LOAN TO VALUE RATIOS

Unlike traditional real estate transactions whereby the loan to value ratio, or the maximum loan amount, of a real estate mortgage loan is determined by an appraisal, the VA manufactured housing loan guaranty program (home only, not land) as well as the FHA and conventional loan programs have utilized the wholesale price or manufacturer's invoice to the purchasing retailer to establish the maximum loan amount for guaranty purposes. Thus, of course, the actual or real cost of the manufactured home to the retailer is a critical item in determining the maximum loan amount. The VA defines "manufacturer's invoice cost" as:

> "that figure shown on a document acceptable in form and content to the Administrator issued by the manufacturer which represents the wholesale price of a specifically identified mobile home including any furnishings, equipment and accessories installed by the manufacturer, which document is certified as the true manufacturer's invoice for that particular mobile home and which separately states the amount of freight or transportation costs charged to the dealer, if any." 38 CFR Sec. 36.4202(k) (1984).

In addition through its Department of Veteran's Benefits, DVB Circular 26-79-34 dated November 9, 1979 the VA requires the following certification on each manufacturer's invoice:

> "The undersigned certifies that the manufacturer's invoice price shown on this invoice reflects the dealer's cost at point of manufacture, exclusive of any and all freight or transportation charges and, **excepting discount based solely on volume purchase**, net of any and all discounts, bonuses, refunds, rebates, prizes or anything of value which will inure to the benefit of the dealer at the time of purchase or at any future date." (emphasis added)

Department of Veteran's Benefits, DVB Circular 26-79-34 dated November 9, 1979 also defines a volume rebate as "an established company marketing practice offered to all dealers on an equal basis for volume purchases over a stated period of time". However, rebates or discounts on single units or "small volume purchases" are not considered eligible rebates.

POINTS PROBLEM

A maximum loan amount determined as a percentage of the wholesale invoice creates a real problem when points are required to be paid to the mortgage lender at the closing. Why are points necessary? Frankly, Mr. Chairman, the manufacturers and retailers of manufactured housing would be most happy if "points" went away and were never required. However, we are told by the mortgage lending institutions that the differences in the real, actual cost of money which they buy and in the simple interest

rate on the mortgage loan require the payment of "up-front" points. This, of course, becomes a very critical factor in a program where the rate of interest to the purchaser is capped or fixed and the cost of money is substantially greater than the contract interest rate.

For some reason -- which is almost magical in nature -- appraisals of residential real property always seem to accommodate, and adjust for, the points situation. Where do homebuilders get the funds to pay points, to buy-down rates. Obviously, from the proceeds from the sale of the home. The points and buy-down funds are a part of the builder's cost of the home. And presto! The appraisal for the maximum loan amount, the loan to value ratio, is sufficiently high for the veteran to pay nothing down or make a minimal down payment.

Is it "illegal" for a home manufacturer to pay the points required by a mortgage lender? Must the manufacturer pay the lender directly -- or can the manufacturer reimburse the retailer for the payment of points? We believe this benefits the veteran purchaser of a manufactured home in the same manner as in the purchase of a site-built home, and we believe that the Veterans Administration regulations should be clarified or interpreted to allow such payments for points.

DEFINITION PROBLEMS

"KICKBACKS" -- "PACKS" -- "INVOICE PADDING" -- "REBATES" -- "VOLUME DISCOUNTS" -- "SALES INCENTIVE PLANS" -- "VOLUME ENHANCEMENT PROGRAMS"

Mr. Chairman, in our opinion, one of the primary problems in discussing the questions relating to invoicing practices within the manufactured housing industry is with reference to the definition of various terms and what they mean. For example, the word "kickback" obviously has an illegal connotation and certainly should not be condoned. Also, the phrase "invoice padding" connotes something of a fraudulent type of practice. The term "rebate" could be applied to an established company marketing practice which was perfectly legal, or perhaps it could also imply a practice that was deceptive. However, there certainly are various "volume discount" programs and "volume enhancement programs" which are perfectly legal methods of promoting competition in the marketplace in the sale of any product, including manufactured housing.

There is a substantial amount of case law which relates to various volume discount programs and multiple tiers of pricing by manufacturers of various products. Thus, the issue of different price structures for the purchase of certain volumes of any commodity has been substantially litigated and has become a legitimate marketing practice to enhance competition in this

country. Just one example: A number of the so-called "fair trades acts" passed by state legislatures have been invalidated by the courts because of the patently adverse effect on competition. We can all recall when the question of whether or not large volume discount stores could sell certain appliances, ie., name brand appliances, when the manufacturer of that particular name brand might have an authorized small dealer within the same city or community. We are all aware of the issues relating to "small" vs. "large" retail operations; and, of course, we are aware of the fact that large discount chains are able to buy merchandise from manufacturers of various commodities on a volume discount plan or on a discounted price basis.

Even the federal anti-trust statutes recognize the validity of volume discounts. The Robinson-Patman Act acknowledges discounts, rebates, allowances, advertising service charges as lawful when such are offered on a non-discriminatory basis to competitors "in respect of a sale of goods of like grade, quality, and **quantity**." (Emphasis added; see 15 U.S.C. Sec. 13(a).)

NMHF believes it is very important for the Subcommittee to consider the fact that volume discounts are simply an established, perfectly legal, and valid form of competition in the United States; provided that the volume discounts are applied in a non-discriminatory manner and are available to all competitors purchasing goods of like grade, quality, and

quantity. Also, it should be remembered that the VA circular (DVB 26-79-34) contained the phrase "...excepting discount based solely on volume purchase...". This circular also states that rebates on single units or small volume purchases are not considered eligible rebates.

WHAT CONSTITUTES "SMALL VOLUME PURCHASES"

Much of the current investigation by the Inspector General, we suspect, is involved with interpretations of what constitutes a legitimate volume discount and what is a "small volume purchase". There is no interpretative problem with a rebate on a single unit (unless perhaps in connection with the payment of points as previously discussed). However, there is no specific definition of the term "small volume purchases" in the VA home loan guaranty regulations. Thus, home manufacturers faced with vigorous competition have been forced to make their own interpretation of "small volume purchases" in connection with the establishment of legitimate volume discount plans to meet the regulations.

How many homes must be purchased by a retailer so that the aggregate is **not** "small volume"? Three, four, six, ten, twelve -- or $100,000 worth, $300,000, $500,000? Over what period of time? One month, a quarter, one year? These are the questions which manufacturers have had to answer without the benefit of any guidance from specific regulations. Thus, unfortunately, many

manufacturers today are finding that their volume discount programs -- which they sincerely believed were properly within the scope of the VA circular -- are being challenged by the investigators and auditors from the Inspector General's office.

A SPECIFIC EXAMPLE OF ONE MANUFACTURER'S INVESTIGATION

To emphasize this problem with interpretation of what constitutes "small volume purchases", we would like to cite a specific example of the investigation of one Texas home manufacturer. This is an **actual** situation -- it is **not** hypothetical.

Let me describe the program for you. In order to qualify for a specified volume discount, it was necessary for a retailer to purchase a minimum of twelve homes per year. There was no specific criteria with regard to the timing of each of these purchases, just the requirement that a total of twelve homes would have to be purchased within twelve month intervals. This company had a policy of paying an "advance" on the volume discounts due to retailers on an incremental basis following the sale of one home and when another home was purchased. If a portion of the bonus plan had been advanced to the retailer by this home manufacturer prior to the expiration of the twelve months period, **and** the retailer failed to qualify from the standpoint of the volume purchase of at least twelve homes during

such period, the home manufacturer would recover the amount of the advance from the retailer (if still in business).

Following some of the rather substantial publicity released by one spokesperson for the Veterans Administration, a home manufacturer in Texas received a subpoena from the Inspector General's office which was extremely broad in scope and content; it required production of substantial books and records which were not in the least relevant to any inquiry into the manufacturer's volume discount program. However, after consultation with the IG investigator, this home manufacturer voluntarily agreed to open its books and records for investigation and examination at its principal office. The investigation and examination was conducted over a period of eight work days during February and March, 1985.

By letter dated March 20, 1985, signed by the Director of the Waco, Texas Regional Office of the Veterans Administration, this Texas home manufacturer was summarily terminated from participation in the manufactured home loan guaranty program for the stated reason that "... Company has engaged in the practice of including dealer unit rebates in the invoice price of homes sold to veterans..." and that "... this practice is unfair or unduly prejudicial to veteran purchasers and that their (home manufacturer's) invoices can no longer be relied upon as true representations of the cost of manufacturing the homes." In other words, this home manufacturer was allegedly guilty of

paying discounts on homes purchased by retailers which were either "small volume purchases" or on single units. Because the Veterans Administration and this Texas home manufacturer had exchanged letters in May, 1981, relating to its volume discount program and answering questions asked by the VA (and inviting additional inquiry if there were further concerns or questions), the principal officers of this home manufacturer were very upset. They contacted and met with the congressman requesting that his office attempt to determine the actual facts or the basis on which the VA allegations stated as the reason for termination were founded. These principals were later advised by the congressman's office that the VA would not give the congressman any information because "the matter was under criminal investigation".

Thereafter, pursuant to the VA regulations, the manufacturer requested an administrative hearing for the purpose of securing reinstatement. On June 25, 1985, a hearing before a three-person panel was convened by the Veterans Administration to consider the request of the home manufacturer for reinstatement of its homes in the VA manufactured housing loan guaranty program. The three-person panel was convened by authority of the Chief Benefits Director of the Veterans Administration.

Naturally, the allegation of the Inspector General was that the company had engaged in a practice of including dealer unit rebates in the invoice price of homes sold to veterans and that

such practice was unfair or unduly prejudicial to veteran purchasers and that the certification of the manufacturer relating to bonus program disclosures (except for volume rebates or discounts) had not been accurate. Specifically, the allegation was that the home manufacturer had included rebates or bonuses in invoice prices to retailers which resulted in overstated or inflated invoices because the program was on a unit basis and not on a volume discount basis as required by the Veterans Administration.

After a full and complete hearing (the transcript and record of the hearing comprised 119 pages), the three-person panel found as follows:

> "Without Veterans Administration participation or review, ... established a suitable plan for rebate payment including appropriate criteria."

Thus, after eight full days of the investigations of the books and records of this Texas home manufacturer and a determination by the Inspector General's Office that it had been including single unit or small volume rebates in its invoice prices, the three-person panel found that the manufacturer had established a suitable plan.

However, the panel did find that the company had been negligent in not administering the criteria for the plan in five instances. (The company's counsel, however, introduced evidence that indicated the actual number was three.) Thus, in either three or five instances out of the many hundreds of sales made to

retailers over a five year period who sold the homes to veterans through the VA home loan guaranty program the manufacturer failed to enforce its criteria.

Thus, the allegation in reality was that the home manufacturer had failed to recover the discount advance from either three or five retailers. The transcript of the administrative hearing reflects a stipulation that this particular home manufacturer had "hundreds of dealers" (retailers). This particular manufacturer also constructed and sold substantially more than ten thousand (10,000) HUD-code manufactured homes in the five years covered by the investigation. The records reflects that the manufacturer did **not**, in several cases, pay a volume discount to retailers who had **not met** the stated volume criteria, and it also reflects that the manufacturer had secured a judgment against one of the five retailers (from the IG report) for the advance which had ultimately not been earned by the retailer.

Query: Of what is this manufacturer guilty? From reading the transcript and record of the administrative hearing, a reasonable person can only conclude that the manufacturer's invoice certifications were made in good faith relying on prior correspondence with the VA. There was no evidence of intent to defraud. However, this Texas home manaufacturer is still (as of the date of this hearing) terminated from the manufactured home loan guaranty program because there was some evidence of

negligent administration of an acceptable, legally valid (as found by the VA panel), volume discount program in either three or five instances. We submit that this type of "administration" problem could be corrected through appropriate guidelines issued by VA. Certainly, this is **not** criminal conduct.

REBATES AND DISCOUNTS NOT VOLUME RELATED

We believe that the current investigation actually involves various types of rebates or discounts to retailers which may not be volume related, but which otherwise may be legally valid. The real inquiry involves whether or not the manufacturer's invoice certification should have been placed on the invoice without actual disclosure of the particular rebate or discount.

Let's look at some examples of these types of invoicing practices.

-- Because of tremendous competition in a given market area, a retailer selling a manufacturer's home is rapidly loosing its traditional market share. Naturally, both the retailer and manufacturer are concerned and, thus, work out a special advertising rebate program for each home purchased by the retailer from the manufacturer. This type of rebate is not illegal, **per se**, but is not based strictly on volume.

-- Retailer "A" tells one of his supplying manufacturers "X" that manufacturer "Y" is offering retailer "B" a special sales incentive rebate on each home purchased during the last quarter

of the calendar year and requests the same type of sales incentive rebate. If manufacturer "X" agrees to meet this vigorous competition, then both manufacturer "X" and "Y" are engaging in discounts which may not meet the current VA criteria -- however, these discounts have a volume relationship and may otherwise be non-discriminatory.

These are examples of invoicing practices which may violate the specific VA requirements for invoice certification by the manufacturer.

However, as will be pointed out later in this statement, the veteran would not necessarily be injured by such practices.

MANUFACTURER'S INVOICE EFFECT ON SALES PRICE

Generally speaking, the manufacturer's invoice on comparable homes has little effect on the sales price of the home because of competition. Naturally, the retailer must recover the cost of purchase of the home, other costs of operations and administration, and some profit in order to continue in business. In general, legitimate volume discounts and non-volume related rebates **primarily** affect the amount of the required down payment.

We would call your attention to the three tables which appear at the end of this statement -- and which we have distributed for convenient reference in separate sheets.

In Table One, an actual example of a VA guaranteed loan transaction is used calculating the maximum loan amount for

guaranty in accordance with current VA regulations. You will note that certain actual costs of retailer-added options are also eligible for the 120% calculation. Also, please note that even though the freight on the home (from manufacturer to retail sales center) was $600, the regulations limit this figure to $400 for calculation of the maximum loan amount. The retailer's installation costs (delivery to home-site, foundation preparation, blocking, anchoring, etc.) are also limited to $400 for a single section home, although the retailer's actual costs were $800.

In Table Two, we have calculated the actual costs to the retailer in connection with the sale of the home. Again, this is a specific example and not just a hypothetical situation except for the basis of operating and administrative costs as reported by Robert Morris and Associates. This figure will, of course, vary somewhat depending on the volume of sales achieved by the retailer versus fixed operating costs which do not fluctuate by virtue of the number of sales or gross sales amounts. The actual retailer costs in this example are $21,155.

In Table Three we have set out two examples. In Example One there is no special non-volume related rebate. Based on a sales price of $21,500 to meet tremendous price competition, the retailer will make a profit of only $345. However, because of the VA maximum loan amount as calculated, the veteran will have to make a down payment of $2,465 -- or 11.47%. To most veterans,

this seems like a very high down payment because they are accustomed to the site-built homebuilder's advertising "100 down" or "nothing down" to veterans.

In Example Two in Table Three, we show the effect of a special non-volume related rebate in the invoice. The sales price is the same, and the retailer's profit is also the same -- but the retailer can undercut the competition by only requiring a $65 down payment -- 0.30%. In this example, the veteran is not discriminated against nor actually injured in any way. In Example Two, the veteran simply saved $2,400 ($2,465 minus $65) in down payment which was added to the mortgage loan ($19,035 loan in Example One; $21,435 in Example Two--a difference of $2,400 in down payment).

However, while the veteran is not in any way injured in this example, the Veterans Administration is actually guarantying $2,400 more than allowed by the regulations. In addition, the retailers and manufacturers which are not involved with special non-volume related rebates are injured because of this type of competition.

VETERANS EXPECT "NO DOWN" FINANCING

Regardless of the original intention of the legislation or the VA in administering the home loan guaranty program -- both for site-built homes and manufactured homes -- the average veteran perceives that these programs are "no down" or require a

very minimal down payment. Because of this real perception most veterans would believe that the retailer in Example One in Table Three was a "crook". How can this retailer possibly require a $2,465 down payment; obviously it's a "rip-off". On the other hand the veteran dealing with the retailer which has received a form of special rebate and charges only $65 down will be perceived as being straightforward and knowledgeable about the VA loan guaranty program.

Thus, retailers in a very competitive market who do not receive non-volume related rebates or discounts suffer competitive harm.

CONCLUSION

In conclusion, Mr. Chairman, we thank you for this opportunity to testify on behalf of the retailers of manfuactured homes across this nation as witnesses for the National Manufactured Housing Federation.

In brief summary:

1. We commend the Veterans Administration for its administration of the manufactured housing loan guaranty program. We deplore any type of deceptive acts or practices in which any member of the industry might be engaged.

2. We regret the unfortunate publicity which has implied that all or a substantial part of the industry is involved in "kickbacks" and "invoice padding" which is simply not true.

3. The present VA regulations do not define what constitutes "small volume purchases" which are excluded in the regulations from being included in volume discount programs; thus, manufacturers have been forced to guess at the correct interpretation.

4. Legitimate volume discounts are not "kickbacks" and are not fraudulent; rather, they enhance competition in the manufactured housing industry just as in other industries.

5. Special non-volume related rebates do not necessarily injure the veteran but always have a serious adverse effect on competition and can increase the VA maximum loan guaranty.

6. The vast majority of current repossessions of manufactured homes are a direct result of the present economic situation in this country.

RECOMMENDATIONS

1. That the VA manufactured home loan guaranty program be continued because of its great benefit to veterans.

2. That the "small volume purchase" interpretation question be resolved by the Veterans Administration, and that the VA issue regulations which make it clear that manufacturers are authorized to pay all or any part of up-front points required by paying either to the lender or by reimbursement to the retailer upon submission of proof of payment.

3. That a "Truth-in-Invoicing Statement" -- such as that

developed by the Manufactured Housing Institute be promulgated, hopefully with the blessing of The Justice Department that such statement does not violate current anti-trust statutes nor injure competition.

4. That the Veterans Administration be expressly authorized (or possibly directed) to establish an alternative appraisal system for determining the maximum loan guaranty amount for manufactured homes in addition to the percentage of wholesale invoice method so that the latter can gradually be eliminated over a period of time when the appraisal system is fully developed.

5. That the Veterans Administration be authorized (or perhaps directed) to establish regulations which will substantially encourage the sale of manufactured homes, where the veteran has defaulted on the loan, in place at the homesite rather than having to move the home to another site.

Respectfully submitted,

National Manufactured Housing Federation
1015 15th Street, N.W., #1240
Washington, D. C. 20005
Telephone: 202/789-8690

By William D. Beville
and Will Ehrle

TABLE ONE

CALCULATION OF MAXIMUM LOAN AMOUNT FOR VA MANUFACTURED HOME GUARANTY

INVOICE COST TO RETAILER		$12,700
--Less Freight Included		(600)
--Less HUD Label Fees		(50)
--Less State Association Dues		(50)
INVOICE COST FOR CALCULATIONS		$12,000
ACTUAL INVOICE COSTS TO RETAILERS FOR ADDED COMPONENTS (LESS ANY SALES TAXES PAID)		
--cost of tie-down anchors	$ 250	
--cost of air conditioning	1,240	
--cost of skirting	350	
--cost of washer/dryer	560	
Total Components	2,400	$ 2,400
TOTAL ACTUAL INVOICE COSTS FOR CALCULATION PURPOSES		$14,400
$14,400 times 120%	=	$17,280
add actual freight (not to exceed $400 for single section)	=	400
add actual sales taxes paid	=	955
add retailer installation (not to exceed $400 for single section)	=	400
TOTAL MAXIMUM LOAN AMOUNT		**$19,035**

TABLE TWO

RETAILER'S ACTUAL COSTS OF SALE TO VETERAN

INVOICE COST OF HOME	$12,700
COST OF ANCHORS	250
COST OF AIR CONDITIONING	1,240
COST OF SKIRTING	350
COST OF WASHER & DRYER	560
SALES TAXES	955
Subtotal	$16,055
RETAILER COST OF TRANSPORTATION TO HOMESITE; INSTALLATION OF HOME ON BLOCKS, PIERS, ETC.; LEVELLING OF HOME; INSTALLING ANCHORS AND SKIRTING; FINAL CHECKS & TESTS OF PLUMBING & ELECTRICAL SYSTEMS	$ 800
Aggregate Cost of This Sale	$16,855
OPERATING AND ADMINISTRATIVE COSTS OF SALES (COMMISSIONS, INVENTORY INTEREST EXPENSE, OFFICE OVERHEAD, WARRANTY SERVICE, INSURANCE, STATE & LOCAL PROPERTY TAXES, ETC.)	$ 4,300***
TOTAL COSTS OF SALE	$21,155

***Based on a survey of retailers by Robert Morris Associates, the average operating and administrative costs for all retailers surveyed represented 20% of the retail sales price. Naturally, it will vary from retailer to retailer depending, to some extent, on sales volume. Robert Morris Associates is a nationally known organization which gathers and compiles statistical data and information for use by lenders, financial institutions and financial analysts.

TABLE THREE

EXAMPLE ONE

A.	Retail Sales Price to Veteran	$21,500
	Less Total Costs of Sale (Table Two)	-21,155
	Retailer Profit (Profit % of Sales Price: 1.6%)	$ 345
B.	Veteran's Cost of Home	$21,500
	Less Maximum Loan Amount (Table One)	19,035
	Down Payment Requirement of Veteran (Down Payment % of Sales Price: 11.47%)	$ 2,465

EXAMPLE TWO

NOTE: Invoice is increased by $2,000 which is a special advertising discount in the particular market area. It is a non-volume related rebate. Maximum loan amount in Table One is recalculated using the invoice increased by $2,000.

A.	Retail Sales Price to Veteran	$21,500
	Less Total Costs of Sale (Table Two Plus $2,000)	23,155
	Retailer Profit (Loss)	(1,655)
	Retailer Special Rebate	2,000
	Actual Retailer Profit (Same as Example One A.)	$ 345
B.	Veteran's Cost of Home	$21,500
	Less Maximum Loan Amount (Recalculated With Increased Invoice)	21,435
	Down Payment Required of Veteran (Down Payment % of Sales Price: 0.30%)	$ 65

Written Testimony

on behalf of the

Association for Regulatory Reform

by

Danny D. Ghorbani, President

Before the

Housing and Memorial Affairs Subcommittee

of

House of Representatives

Veterans Affairs Committee

Washington, D.C.
September 12, 1985

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Association For Regulatory Reform

1331 Pennsylvania Avenue, N.W., Suite 524 • Washington, D.C. 20004 • 202/783-4087

A. Introduction

This is the written submission to the Housing and Memorial Affairs Subcommittee of the House of Representatives Veterans Affairs Committee of the Association for Regulatory Reform. ARR is a non-profit trade association which was organized in July of this year to represent the interests and views of manufacturers, especially those in the manufactured housing industry, concerning regulations at the federal level. Because our members represent an important segment of the production available in the manufactured housing industry, the wide-spread publicity this year about possible fraud in connection with Veterans Administration's insured loans is of grave concern to our members and to all citizens. We believe that a question of such singular importance deserves close attention in order that fraudulent practices be stopped and to ensure that an entire industry not be mislabeled or penalized for practices which are not fraudulent.

The Veterans Administration has done an outstanding job since the inception of the program in assisting veteran home buyers. With its companion, FHA, the Veterans Administration has enabled millions of Americans to own their own homes, Americans who would otherwise not be in

a position to have the security represented by an affordable house. The manufactured housing industry has benefitted from the Veterans Administration program although the number of homes sold with VA insurance has been generally less than 5% of total sales. For several years manufactured housing industry shipments have hovered around the 300,000 mark, but one out of every three homes sold for less than $50,000 has been made in a factory. The impact of the Veterans Administration program, therefore, can be seen because manufactured homes are an important choice for low and moderate income Americans.

The manufactured housing industry is unique. It consists of a small number of manufacturers, perhaps less than 300, but as many as 10,000 dealers strung out in a network covering all of the United States. The industry is most competitive. There are no franchises. Some manufacturers, particularly in the southeast, have many company-owned dealerships. Nearly all dealers sell the products of several manufacturers in a state of vigorous competition.

The tight credit supply and the high interest rates of the 1970's and 1980's have had a disproportionate effect on the low income buyer. Not only buyers have been affected but financial institutions have been severely stressed by volatile interest rates. As recently as Saturday, September 7, 1985, the Washington Post carried a series of articles on the desperate attempts by financial

institutions to adapt to the changing environment, most recently graphically illustrated by the domino collapse in the Maryland thrift industry. Savings and loan associations are an important source of financing for manufactured housing throughout the United States.

In this climate it is easy for notions to become prevalent which have no valid foundation such as the idea that the manufactured housing industry is engaged in a massive fraud upon the Veterans Administration. There have been several news releases issued by the Veterans Administration which could be interpreted to that effect. With respect to one important issue, the current ferment about the financing of housing has caused, in our opinion, a retroactive interpretation of the Veterans Administration certification stamp required in its insurance program. The current meaning attached by some to the Veterans Administration certification stamp is revisionist history.

Later in this submission we will analyze in detail the circumstances under which the certification stamp was designed and issued. But the principal themes of our submission are these:

(1) The VA certification requirement which was published informally in a VA circular letter without an opportunity for comment and without explanation is ambiguous and confusing and not properly the basis for criminal prosecution.

(2) Most manufacturer invoices <u>do</u> comply with the requirements of the certification when that certification is understood in the context of VA's stated purpose for issuing that circular. That purpose was to prevent dual pricing practices in the VA manufactured home program because

veterans should not be charged a different price than other purchasers. Recent evidence goes a long way towards proving that "rebate" was used in a very special way in the circular letter.

(3) Industry invoicing practices which recently have been alleged to constitute illegal rebates are not illegal because they do not result in dual pricing. Moreover, the concept of "rebate" current in the industry when the circular letter was issued was different than the meaning now attributed to the word by the VA. For example, the invoicing code agreed upon by the industry at that time defined a "rebate" as an attempt to increase the invoice above list price with a return of the excess to the dealer.

(4) The invoice practices which are now construed as improper have been tacitly approved thousands of times by VA during the six year period in which the certification has been in effect. These invoicing practices, which are permitted in every major industry, should not now, on the basis of an ambiguous certification, be used to justify allegations of fraud against an entire industry.

Financing during a time of high interest rates is a complicated issue and because it involves esoteric words common to a segment of the housing industry, fairness requires a close examination of the facts. No illegal or improper practices were followed in the opinion of ARR when manufacturers assisted the dealers. It is not generally understood, for example, that in the manufactured housing industry the sale by the manufacturer to the dealer takes place long before the purchaser chooses a financing method and thus the manufacturer has no way of knowing that a Veterans Administration sale is involved. The sale to the dealer is completed and paid for in some cases six months before the sale by the dealer to the purchaser.

We will analyze below in more detail the industry conditions which affected the financing of manufactured housing and the responsibilities of the manufacturers not only to the dealer but to the purchaser. We will show that the Veterans Administration stamp is unusually ambivalent and misleading. We have recently uncovered evidence that proves that the certification stamp has not been violated because its purpose was to prevent duality in pricing, i.e., a different higher price for veterans not to forbid normal business incentives to the dealer. Finally, we will show that the lending institutions have now taken steps to solve the problem created by high interest rates by increasing the allowable amounts to 125 to 130% of invoice from 110 to 115%.

B. Industry Conditions Affecting Financing

Beginning in 1974 representatives of the manufactured housing industry met with representatives of FHA and VA to discuss the failure of each agency's mobile home financing programs to gain widespread support. The main stumbling block to the success of these programs was identified as the need for payment of marketing "points" on loans under such programs. These "points" were payable as a result of the maximum interest rates on such loans being below conventional market rates. At that time neither the consumer nor the mobile home dealer could pay such "points" under the VA and FHA programs. Thus it was left to the

manufacturer to pay the "points." As interest rates began to rise the problem was exacerbated and lenders began to demand as many as 20-25 points. Lenders also began to require that the manufacturer commit to the payment of retail "points" prior to purchase of the home by the dealer.

In this atmosphere, FHA (in 1978) opined that, while the dealer could not pay the "points" directly, the manufacturer could deduct the payment of the "points" from the dealers volume bonus payment. The dealer would thereby pay the "points" in an indirect manner. This facade was dropped the next year and the direct payment of "points" by the dealer authorized.

The payment of "points" directly by the manufacturer was a wholly unworkable system. The manufacturer sells homes to independent dealers throughout the country. A large manufacturer may have thousands of dealers who sell products made by several manufacturers. Homes are sold to the dealer for stock or are ordered for a specific retail customer. Stock units may not be resold for a year or more to retail customers. During that time interest rates and "points" may accelerate and the manufacturer who priced his products to the dealer in January may be faced with a substantial, unanticipated loss on the home in December. Further the manufacturer has no control over the terms of the sale by the dealer to the retail customer or an ongoing relationship with the source of financing for the retail purchase (often a local bank or a retail financer). Payment

of the points by the manufacturer requires the manufacturer to become a party to the retail sales contract, a position contrary to general industry practice. It was in this atmosphere that payment of retail points by the dealer became a reality.

Because of the low profit margins realized by dealers on government as well as conventional programs, the dealer is unable to fund the payment of "points" from his general revenue. Quite aside from the "points" now demanded, the dealer was required to fund service and "set up" of the home. The VA allowances for such items were woefully low imposing further strains on the dealer structure. Does the manufacturer provide the funds by gearing its price to the type of retail financing program anticipated on a specific retail sale which may not take place for six months? No, that's impossible. Can the manufacturer or the dealer create a special price for FHA or VA deals:? No, that's illegal. What alternatives are left to handle the "points" problem? The manufacturer can provide the dealer with funds on a uniform basis applied to all sales, which is designed to allow the dealer to pay the "points" on the retail sale no matter what retail financing program is chosen by the consumer and dealer. Thus a single price is maintained, the variable "points" are provided for and the FHA and VA programs are viable while an independent dealer network is maintained. This was the solution

developed and utilized by many manufacturers in varying forms in the Winter of 1979-80.

This solution did not violate the VA certification because it did not result in dual-pricing. This was the system described on at least one occasion to VA officials in the Spring of 1980. The officials termed the system "cogent" and had apparently accepted the system at that time.

This historical background and logical development were ignored by the VA in making its current determination that the system violates the certification.

During 1979 and 1980, the traditional financing arrangements for retail sales of mobile homes were becoming increasingly chaotic. Interest rates had soared on short-term monies to 22% and long-term rates were virtually as oppressive. Over a 7- or 8-year period, premiums which had been paid for many years by financial institutions to dealers were eliminated and replaced instead by so-called "placement fees" to be paid by dealers to financing institutions for granting loans to purchasers. Incentives to dealers for placing insurance which had amounted to hundreds of dollars per sale had also been eliminated. The impact on the cash flow and viability of the dealer structure was profound. The dealer, as an example, had gone from the situation where he received as much as $1,100 for placing the loan at the time of sale to the point where he was paying 10 to 20 "points" to the lender. This resulted in a

difference of $1,800 to $2,500 in the dealer's cash flow on a low end minimum invoice home selling for $10,000 or less. Another factor, state usury laws, complicated the picture. Often, the reason for the placement fee was an attempt by the finance company to obtain a retail interest rate that appeared lower or equal to the top limit of legal state rates under usury laws but in effect was higher. Lenders pressured Congress to solve state usury limits and eventually state usury laws were preempted by the Federal Government on financing obtained through use of the Federal banking system.

Beginning in 1976, the manufactured housing industry went into a recession which exists to this day. Thousands of dealers and scores of manufacturers have gone bankrupt or ceased doing business.

C. Responsibilities of Manufacturers After Sale to Purchaser

Manufacturers never sell to retail purchasers. The manufacturer pre-sells the home to dealers usually before production of it begins and the manufacturer does not know to whom the dealer will sell the house or how it will be financed. After the financing process the manufacturers may or may not be asked to verify the invoice price depending on the terms of retail sale.

Approaching this problem in another way the State of Ohio in 1980 attempted to impose a statutory service requirement for manufacturer reimbursement of dealers for "set-up" and service. Manufacturers have both a practical

and legal obligation to make certain that the dealer has the resources required to cover his functions and in addition to fulfill manufacturers obligations under the HUD Code and the National Manufactured Housing Construction and Safety Standards Act of 1974 (Title VI of Pub. L. 93-383, 88 Stat. 700, 42 U.S.C. 5401, et seq.).

D. The Veterans Administration Certification Stamp Is Patently Ambiguous and Confusing

The Veterans Administration began to require a stamp on invoices used as part of the VA guaranteed loan system in 1979. This stamp was described in a general letter to the industry. (See attached letter of Dorothy Starbuck, Chief of Benefits.) However, the circular letter was never sent to manufacturers nor published in the Federal Register. The VA never issued an explanation or instructions about the stamp other than the wording of the letter.

The certification stamp is unfortunately not self-explanatory. To appreciate this one must recognize what other lenders and U.S. agencies require. The U.S. Department of Housing and Urban Development, e.g., has no such certification. In fact, the definition of "Invoice Price" used in the context of GNMA transactions stated unequivocally that an "invoice price" is merely the sum of the charges on the invoice. The industry knew of and frowned on "rebates" but the term "rebate" in this industry had a specific meaning at the time the VA stamp was issued. The national trade association for manufacturers of mobile

homes had adopted a Uniform Invoicing Code to which its members subscribed. The definition of "rebate" in that code (see attached copy) is entirely different from the definition which it is understood the VA now is using. "Rebate" according to the then current industry practice in 1979 involved adding a sum to the invoice above the published price and returning that sum to the dealer. This was forbidden under the industry code unless disclosure was made. List prices were prevalent in the industry with prices the same to all dealers. But there was no industry or government restriction on what the manufacturer did with his general revenue derived from sales at published list prices.

The VA in its certification in the Winter of 1979 appeared to be concerned with preventing sales at prices different from list prices to veterans. Such special prices were illegal. Although the term "rebate" at that time clearly referred to dual pricing, the VA seeks to impose a a new definition of "rebate" retroactively. The VA is attempting to change U.S. industrial practice with respect to the ability of commercial enterprises to control their profit and general funds.

The certification, moreover, is highly ambiguous. First of all it is not directed to an agency of the U.S. Government nor does it refer to or invoke a U.S. criminal statute as the penalty for its violation.

Rather than clear words necessary for criminal sanctions, the certification states only that certain items be "reflected" in the invoice. "Reflect" is not a word of clarity or precision in this context. The next phrase in the stamp "dealer's cost at point of manufacture" assumes an impossible calculation. We must assume the term should be "dealer's price." What costs the dealer incurs when the home is purchased in addition to the invoice price we cannot calculate. The phrase evidently is borrowed from the traditional "manufacturer cost at point of manufacture or point of shipment" common to shipping. Calculation of freight from point of manufacture is usual in certain industries. Computation of "dealer's cost at point of manufacture" simply does not occur in the manufactured housing industry. The "dealers cost" is a published list price payable upon delivery in this industry. No accounting at point of manufacture is ever performed. The certification, then, proceeds to note certain exceptions to the stamp. Unfortunately these exceptions are neither all inclusive or of a class which would give guidance to a certifier. There is no distinction between the significant and the insignificant, e.g., the use of the word "prize." It is not clear whether the phrase beginning with the word "net" modifies the word "volume purchase" or the words "dealer's cost." The entire sense of the stamp could change in that event. Nor were the words ever defined. No attempt was made to deal with spare parts credits, returns of

components for credit, payments for services or credits for damages en route, or other such charges. The certification should have stated that it was not meant to cover transactions for consideration nor for which payments were properly rendered.

The certification ends with an incomprehensible prohibition against manufacturers giving the lender "anything of value which will inure to the benefit of the dealer at the time of the purchase or at any future date." This phrase indicates that the certification operates in the future and not with respect to the sale by manufacturer to dealer which necessarily predates financing, but it does not convey any substantive guidance. This phrase ignores the mechanics of the sale, including the fact that the manufacturer has usually no knowledge of the financing when he sells to the dealer. The language seems borrowed from a conflict of interest not a commercial environment.

That this certification should govern ordinary commercial incentives usual to businesses which have published prices is an impermissible and illogical step.

The inclusion in the Starbuck letter of the prohibition against duality in pricing moreover was a plain indication that it was violation of the prohibition against a special line of products for veterans which was the principal concern of the VA. Only in that context is the stamp logical and intelligible. But the letter is ambivalent even in that prohibition because Paragraph 2

qualifies its stand by the statement that "dual pricing . . . may well be considered . . . unfair or prejudicial to veteran purchasers within the meaning of 38 U.S.C. 1819(k)." The Veterans Administration at that time was apparently not sure that any law was violated.

E. The Purpose of the VA Certification Stamp

The VA with full knowledge of the growing financial confusion in the manufactured housing industry in the late 1970's gave no instructions about its stamp other than the bare words in the letter about duality of pricing. Despite the fact that all major U.S. manufacturers in every major industry have discounts and rebates within established list prices, the VA has now construed its certification stamp in a manner which is inconsistent with approved industrial practices. The VA would limit under penalty of criminal prosecution the manufactured housing industry from industry rebates and discounts which are not criminal in any other industry. A serious question arises whether VA's failure to describe the meaning of this ambiguous stamp and its silence about financial problems was an attempt by the VA to entrap the unwary and to retroactively enforce a concept of criminal conduct which did not exist at the time. Therefore a manufacturer is faced either with allowing the financing of a tiny portion of its sales to change its "rebate" practices for the vast majority of its sales or with answering charges of criminal conduct.

F. VA's Interpretation of the 1979 Circular Letter Has Changed

It has been pointed out above that the VA certification is uncertain and ambiguous. The words were never explained. Attached is the circular letter which announced the policy of requiring the certification stamp in 1979 signed by Nancy Starbuck. The circular letter speaks to the certification in connection with duality of pricing which is forbidden. Duality of pricing means that despite the inconsistencies in interest rates and added "points" on VA guaranteed loans, veterans could not be charged a different price than non-veterans. The industry was faced with a law on duality with sanctions for breaking the law. The Starbuck circular letter relates the certification stamp to duality of pricing. No instructions explaining the Starbuck letter were issued in the Federal Register or elsewhere by the VA. Six years later in 1985 indictments have been threatened for "rebates" against those whose published prices were the same for VA insured and conventionally financed homes. The justification for this position is not in accord with the stamp or the industry practices when it was issued.

In an attempt to discover what the VA really had in mind when it used the Starbuck circular letter in 1979, a Freedom of Information Act request was made to the VA. The request asked whether there were any documents which would reveal what was meant by this circular letter particularly

because of the absence of any clarifying instructions at the time. Although the VA refused to release such information with one exception, that one document demolishes any pretense that the certification stamp was meant to be construed in the manner in which it is now being enforced, i.e., as an independent certification unrelated to duality of price. The current VA interpretation is that the stamp forbids all rebates (other than dealer volume bonus rebates) from the general funds of a company within a uniform published price. The document which was received under the FOIA request was VA Form 20-2 "Justification for Proposed Issue or Report." This document was composed to obtain approval within VA to publish DVB Circular 26-79-34, the Starbuck letter. The document proceeded through the usual chain of command for concurrences and was approved by the Director of the Loan Guaranty Service. Block #4 requires the originator to describe the purpose, i.e., "the necessity, objective and reason for the circular." As the attached copy shows the purpose of the circular was

> To inform stations of the Central Office release of instructions to Mobile Home programs participants warning against dual pricing practices.

At the time of its issuance the VA management considered the certification as a part of the warning against dual pricing. The wording of the certification stamp can be construed logically only with respect to dual pricing and it makes sense where increases and return payments are above the published price but not where the rebates are within the

list price from manufacturers funds. By using added increments above the list price the veteran could be charged a different price than others and dual pricing would occur. Thus, there is a current rush to indict for actions which were not conceived at the time of the circular letter as criminal or as contrary to the stated purpose of the circular. To persist in construing as criminal every relationship between manufacturer and dealer in which money passes either for incentives, rewards, services and credits is completely illogical. The justification stated at that time for the circular letter confounds such an imputation of criminality.

The Veterans Administration, moreover, guaranteed loans when both the VA and the lenders knew of "Dealer Assistance" programs.

G. Aftermath of the High Interest Rates

The realization that a strong dealer structure is essential if homes are to be available to moderate income Americans has been strong in the industry. The lenders also appear to believe that the dealer cannot operate on the low percentage of invoice value which was used as the basis for advances during the sky-high interest days. Recently lenders began to allow 125-130% of invoice. Manufacturers invoice price and dealers selling price have no constant relationship. Dealers are free to price homes at their discretion because in the manufactured housing industry the

market place determines price not manufacturer's cost nor invoice. Moreover, the concept of a manufactured home as a type of vehicle has been discarded by every knowledgeable governmental body. Many of the lending attitudes derived from the days of travel trailers. The courts in every state now recognize the real property character of manufactured homes as adjuncts to real estate. Contrasted with the early years over 95% of the homes produced move only once.

The experience with repossessions and delinquencies in the industry has also been impressive. Until 1985, delinquencies and repossessions experienced continuous decline, at times running lower than site built housing. It is suspected that failure to screen borrowers has caused a high rate of repossession, e.g. the Texas and Mountain States oil boom areas. Failure to move quickly to protect the security in the home itself has also been a constant problem causing losses to insurers and guarantors. Homes have been stripped of appliances by departing buyers but no attempt to prosecute the debts to payment has been made. Nevertheless the financing of manufactured houses continues to attract the same lenders. On the positive side lenders are advancing 125% and 130% of invoice to dealers finally recognizing that the previous limits were harming the integrity of the dealers' function. The financial assistance payments to dealers which were made when loans were restricted to 110% of invoice became less pressing when advances at 125% of invoice were allowed. If the cost of

the dealer function is analyzed and provided for in the financing advance, no special dealer assistance will be needed.

Both FHA and VA have now approved increases in the percent of invoice advanced to the dealer. It is our understanding that the VA has also suggested charging 5 points to the veteran for itself on all transactions in order to liquidate inevitable costs of the guarantee program. Putting restrictions on one part of the program merely results in compensation at another place.

Assisting the dealer to pay the "points" was not a violation of the VA certification and could have been avoided if higher advances had been provided. In any case, the veteran was not subjected to dual pricing by the "Dealer Assistance" programs.

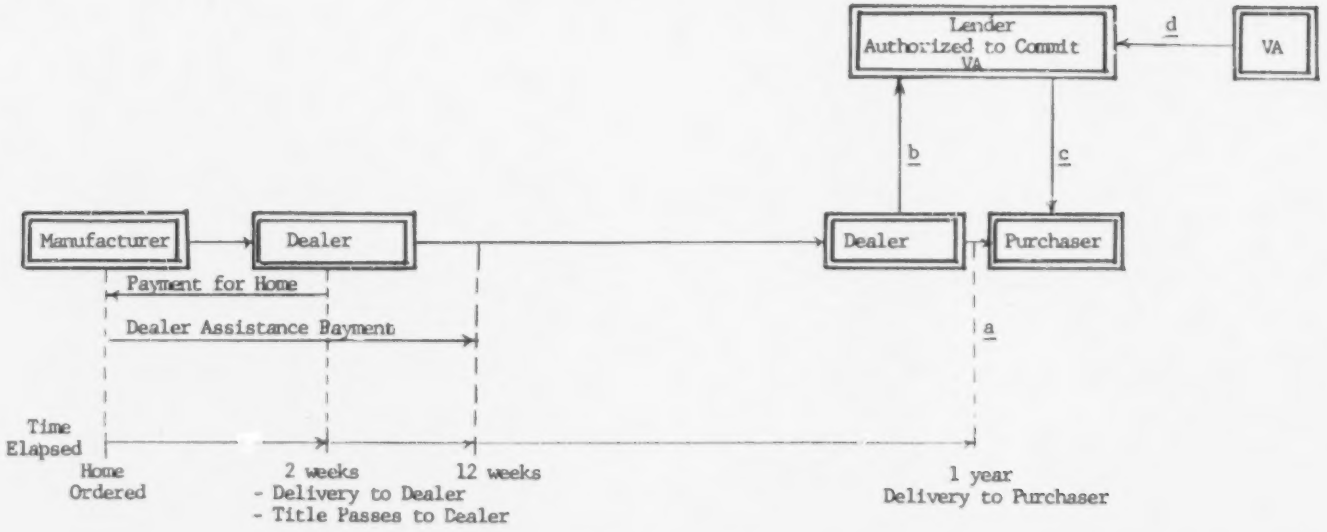
H. Conclusion

Because of the information presented above ARR believes that manufacturers' assistance to dealers to pay "points" did not violate the Veterans Administration circular letter and the stamp required by it.

We appreciate this opportunity to testify before the Subcommittee.

THE SALE AND FINANCING OF A

MANUFACTURED HOME IN THE LATE 1970'S



Notes:

- Dealer volume bonus rebates are usually paid once a year.
- Currently the VA guaranteed loans in the industry covers approximately 3% of the industry's annual production -- about 9,000 homes annually.

Legend:

a - Sale to consumer at dealer's price
b - Manufacturer signs the certification stamp and dealer pays lender the points (as many as 20)
c - Lender loans buyer a 110% of manufacturer's invoice
d - VA guarantees 1/2 of the loan (loan = 110% of manufacturer's invoice + allowances for set up, skirting, etc.)

Department of Veterans Benefits
Veterans Administration
Washington, D.C. 20420

DVB Circular 26-79-34

November 9, 1979

MOBILE HOME MARKETING PRACTICES

1. Mobile home manufacturers producing homes to be sold to veteran-purchasers with loans guaranteed by the VA are required to place the following certification on the face of the manufacturer's invoice, signed by an authorized representative of the manufacturer:

"The undersigned certifies that the manufacturer's invoice price shown on this invoice reflects the dealer's cost at point of manufacture, exclusive of any and all freight or transportation charges and, excepting discount based solely on volume purchase, net of any and all discounts, bonuses, refunds, rebates, prizes or anything of value which will inure to the benefit of the dealer at the time of purchase or at any future date."

VA's definition of a volume rebate is "an established company marketing practice offered to all dealers on an equal basis for volume purchases over a stated period of time." Rebates on single units or small volume purchases are not considered eligible rebates.

2. It has come to the attention of VA that rebates, discounts and dual pricing are possibly occurring in certain segments of the industry. Participants are reminded that violations of VA requirements can result in the imposition of administrative sanctions (38 U.S.C. 1819(j) and (k) and VA Regulations 4233 and 4235 (38 CFR 36.4233 and 36.4235)). In addition, any known false representations made to a Federal agency may result in criminal sanctions.

3. Dual pricing by dealers; i.e., one price to veterans using VA financing and a lesser price for cash or financing other than through VA, may well be considered by VA to be a marketing practice "unfair or prejudicial to veteran purchasers" within the meaning of 38 U.S.C. 1819(k) and lead to the imposition of sanctions by the VA.

4. Copies of this circular are being forwarded by Central Office directly to industry trade associations for distribution to their members.

Copy: Under Pamphlet 26-9

Dorothy L. Starbuck

DOROTHY L. STARBUCK
Chief Benefits Director

Distribution: RPC 2021
FD

The Exact Language of VA Certification Stamp

"The undersigned certifies that the manufacturer's invoice price shown on this invoice reflects the dealer's cost at point of manufacture, exclusive of any and all freight or transportation charges and, excepting discount based solely on volume purchase, net of any and all discounts, bonuses, refunds, rebates, prizes or anything of value which will inure to the benefit of the dealer at the time of purchase or at any future date."

Name Title Date

SOURCE: 22nd Annual Survey Mobile Home Financing
Mobile Homes Manufacturers Association

UNIFORM INVOICING CODE

RESOLVED: That the Mobile Homes Manufacturers Association recommend that each of its manufacturing members adopt the following Uniform Invoicing Code and that all financial institutions and insurance companies demand compliance with the Code by all members of the industry.

1. That all manufacturers furnish financial institutions and insurance companies who request them, price lists stipulating freight practices and current bonus plans, including subsequent modifications thereof.
2. No equipment will be charged on the invoice which is not a part of that particular unit.
3. No invoice will be inflated above published price to include dealers rebate unless full disclosure is made.
4. Each invoice issued by a member or non-member manufacturer should bear the following legend:

   'This invoice conforms to the Uniform Invoicing Code recommended by Mobile Homes Manufacturers Association by resolution adopted July 6, 1966, again ratified on March 18, 1971 and revised March 23, 1972.'

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At the request of the Finance Committee of the Suppliers Division, the MHMA Board of Directors adopted a Uniform Invoicing Code in 1966. Over the years this Code has been amended and strengthened. It was again changed in 1972. The revised Code as then adopted by the Board of Directors reads as it left.

Certainly, any lending institution should give the above matter careful consideration. It has been the practice with most of the major lending institutions to require that the legend in point 4 above be included on the face of the invoice. Customarily, this has been accomplished with the use of a rubber stamp.

JUSTIFICATION FOR PROPOSED ISSUE OR REPORT

A1907

INSTRUCTIONS

A. ISSUE WITHOUT REPORT - Submit manuscript and VA Form 20-2 in duplicate.

B. REPORT OR ISSUE WITH REPORT - Submit manuscript and VA Form 20-2 in triplicate.

C. TELETYPE ISSUE - Submit in triplicate; confirmation copy and VA Form 20-2 in duplicate (in triplicate if report required.)

D. This form will NOT be used for submission of issues requiring the Administrator's approval. Use VA Form 0-4265.

E. ROUTING - Always route to Departmental Publications Control Officer before routing to Chief Benefits Director.

F. When reports control symbol only is required with no printing approval of Departmental Publications Control Officer is not necessary.

SECTION I - JUSTIFICATION AND CONCURRENCES

1A. APPROVED BY DIRECTOR OF SERVICE ORIGINATING ISSUE (Signature and title) | DATE | 2. PROPOSED MEDIUM (Manual, Intrend Issue, etc.)

DATE: 21 1979

P. C. COON
Director, Loan Guaranty Service

DVB Circular 26-79-34

3. SUBJECT

MOBILE HOME MARKETING PRACTICES

4. PURPOSE (Explain fully the necessity, objective, reason for change in existing issue, etc. For a report explain in detail the problems to be resolved and specifically how data will assist in solution. If more space is required, use "Remarks" Section.)

To inform stations of Central Office release of instructions to Mobile Home program participants warning against dual pricing practices.

5. CONCURRENCES

IMPORTANT - Concurrences are to be indicated by signature of Director of Service, Department of Veterans Benefits; Department Heads; Top Staff Officials or their designees. ORIGINATOR, indicate concurrences to be obtained by checking box adjacent to appropriate symbol. Do NOT check (20) unless concurrences are required outside Department of Veterans Benefits.

(√)	SYMBOL	SIGNATURE	DATE	(√)	SYMBOL	SIGNATURE	DATE
X	(20)				(28)		
	(21)				(29)		
	(22)			X	(021)		
	(23)						
	(24)						
X	(25)	(26A4) (264) (265) (26A)				OUT 12-10-79	
	(27)						

NOTE: All original papers pertaining to this issue, such as comments received during coordination, memoranda or letters and all supporting documents must be attached for purpose of obtaining approval of issue and for retention in final history file.

I CERTIFY THAT the attached manuscript is covered by the above concurrences, if any, and is ready for editorial review.

7A. FORWARDED FOR APPROVAL (Signature of Department Publications Control Officer) | 7B. DATE

8A. SIGNATURE OF LIAISON OFFICER, ORIGINATING SERVICE | 8B. DATE

JUDITH H. EAGAN

JOHN T. TURNER

9A. DVB CONTROL NUMBER | 9B. DATE RECEIVED | 9A. APPROVED FOR PUBLICATION (Signature of Chief Benefits Director) | 9B. DATE

DOROTHY L. STARBUCK
Chief Benefits Director

10A. REPORTS CONTROL SYMBOL | 10B. DATE ISSUED

VA FORM AUG 1972 20-2 | EXISTING STOCKS OF VA FORM 20-2 SEP 1969 WILL BE USED. | 508-484

SECTION II - COST

NOTE: Any increase in cost requires coordination with OVB Management and Budget Service

11A. EFFECT ON COST (Check applicable space on each line.)

FACTOR	INCREASE	NO CHANGE	DECREASE
PERSONNEL		X	
TRAVEL		X	
EQUIPMENT		X	
SUPPLIES		X	
OTHER			

11B. EXPLANATION OF COST FACTOR AND ESTIMATE OF INCREASE OR DECREASE (If more space is required, use "Remarks" Section.)

SECTION III - PUBLICATIONS AFFECTED

12A. RESCISSIONS OR AMENDMENTS EFFECTED BY PROPOSED ISSUE (List specifically, including Remote Control Symbol, if applicable)

RESCISSIONS	RESCISSION DATE (This issue) (Check one)	AMENDMENTS
None	☐ JANUARY 1 ☐ APRIL 1 N/A ☐ JULY 1 ☐ OCTOBER 1	None

12B. NEW FORMS REQUIRED BY PROPOSED ISSUE (Include form number and issue date)

None

SECTION IV - DISTRIBUTION

13. DATE ISSUE MUST REACH USING OFFICES TO ACCOMPLISH PURPOSE (Include justification for priority if requested)

11-13-79 (See 3230 for explanation)

14A. DISTRIBUTION (Indicate distribution to be made, i.e., RPC 2050, BOA-1 each, etc.)

RPC 2021
FD

14B. SHOULD ISSUE BE DISTRIBUTED TO HEADQUARTERS, NATIONAL SERVICE ORGANIZATIONS? ☐ YES ☒ NO

14C. SHOULD ISSUE BE DISTRIBUTED TO ACCREDITED REPRESENTATIVES? ☐ YES ☒ NO

14D. SHOULD ISSUE BE DISTRIBUTED TO VETERANS BENEFITS COUNSELORS? ☐ YES ☒ NO

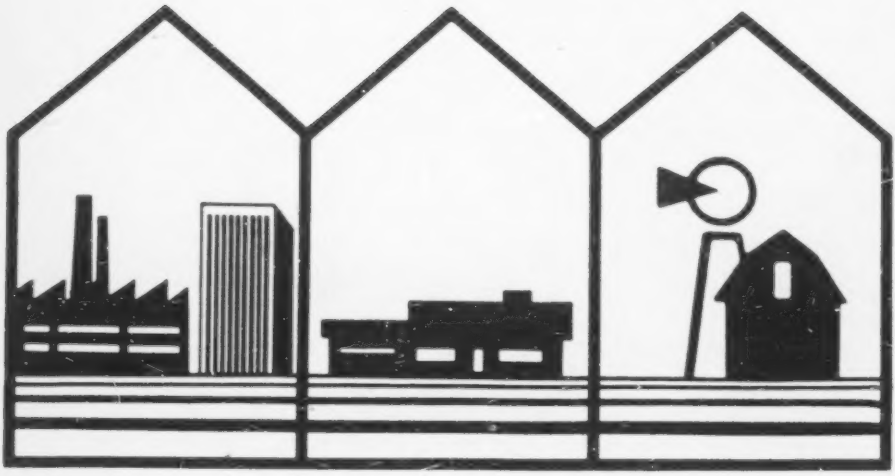
SECTION V - COMPLETE IF ISSUE INVOLVES POLICY OR PROCEDURE

15A. IS THE USE OF THIS POLICY OR PROCEDURE IN AN EMERGENCY COVERED BY EXISTING DIRECTIVES ON EMERGENCY OPERATIONS? ☒ YES ☐ NO (If "No", complete Item 15B)

15B. DATE EMERGENCY POLICY OR PROCEDURE WILL BE SUBMITTED FOR APPROVAL (Must be within 45 days)

16. REMARKS (Include justification for use of Special Issue.)

17A. NAME OF ORIGINATOR OF PROPOSED ISSUE (Type or print)	17B. SYMBOL	17C. ROOM NUMBER	17D. TELEPHONE NO.
Contact: J. Eagan	26A5	379	3486



Statement of the

NATIONAL ASSOCIATION OF REALTORS®

THE WORLD'S LARGEST TRADE ASSOCIATION

TO THE: HOUSE VETERANS AFFAIRS SUBCOMMITTEE ON HOUSING & MEMORIAL AFFAIRS

ON: VA HOME LOAN GUARANTY PROGRAM

BY: DORCAS T. HELFANT, 1986 NATIONAL VICE PRESIDENT and CHAIR OF THE VA HOUSING PROGRAM TASK FORCE

DATE: SEPTEMBER 12, 1985

My name is Dorcas T. Helfant. I am a REALTOR® from Virginia Beach, Virginia, which has one of the largest military populations in the nation. This year I served as a Regional Vice President and will be the NATIONAL ASSOCIATION OF REALTORS® 1986 National Vice President. Also I was appointed to Chair this Association's Veterans Administration Housing Program Task Force.

On behalf of the more than 670,000 members of the NATIONAL ASSOCIATION OF REALTORS®, I want to thank the Chair, Representative Shelby, and members of the Subcommittee for the opportunity to present ways in which REALTORS® can help the Veterans Administration keep the cost down of the VA Home Loan Guaranty Program in order to maintain this important veteran benefit. Before I present to the Subcommittee the recommendations of our Task Force which were recently adopted by the Association's Executive Committee, I would like to thank both the Veterans Adminstration and Congressional staff members for giving us their time and assistance in this project.

During the course of the past year, the financial problems of the VA Revolving Fund and the Administration's proposed increase of the current 1 percent "user fee" have encouraged the NATIONAL ASSOCIATION OF REALTORS® to study and review VA Home Loan Guaranty the program in general but more specifically, the management and disposition of its inventoried properties.

Earlier this year, a group of REALTORS® met with Veterans Administration staff to discuss the various procedures of the VA Home Loan Guaranty Program. The REALTOR® members made the following general recommendations on improving the operations of the system:

- strengthen and standardize its underwriting guidelines;

- implement a review process for quality control of its appraisals; and

- continue implementation of its new case-by-case foreclosure policy. Recognizing that prior to the enactment of the Deficit Reduction Act of 1984, perhaps the single, most expensive drain on the VA Revolving Fund was the excessive volume of VA foreclosures, the NATIONAL ASSOCIATION OF REALTORS® supported Congressional legislation last session to institute a case-by-case, economic benefits foreclosure policy.

The REALTOR® group concluded that the Revolving Fund's current financial deficit could be best assisted by the sale of its inventoried properties which reached a high point this year of approximately 22,000 with an estimated worth of $800 million. Given the expertise of the real estate professional, the REALTOR® group recommended that the NATIONAL ASSOCIATION OF REALTORS® concentrate its attentions on this financially burdensome inventory.

In August, a second group of REALTORS® met with the sole objective to devise a model program to dispose and manage the VA inventoried properties. The Task Force successfully designed a marketing plan which it later reviewed and discussed with VA staff and House and Senate Veterans Affairs staff.

The main purpose of the marketing plan was to develop a system using the REALTOR® structure which would inform the real estate professional of the VA inventoried properties and encourage their participation in the program. The

plan also sought to generate better communications among the local VA staff, the real estate professional, and the potential homebuyer.

The marketing plan envisioned the participation of either a REALTOR® local board or state association in presenting to VA a flexible plan to assist them in the disposition of VA inventoried properties. The appropriate REALTOR® organization would either create or make use of an existing information system. This system would provide interested real estate professionals within a specified geographic area the necessary data to evaluat available VA properties so to accomodate the prospective homebuyer with another option.

This new information system would provide VA with a broader, more industry compatible marketing tool. The information would be delivered to the real estate professional on a cost-plus, differential (i.e. REALTOR® member vs. nonmember) fee basis, with each REALTOR® organization (i.e. local board or state association) negotiating the system costs with the appropriate VA Regional Office. The REALTOR® organization would also provide the real estate professional with all necessary VA forms.

In addition to the information system, a liaison component between the REALTOR® organization and the VA Regional Office was felt to be essential to the success of the marketing plan. Therefore, a VA Advisory Council would be created at the appropriate system level which would be comprised of local real estate professionals and VA regional staff. The Council would assist VA with the pricing of its properties, based on market date; the marketing of its properties; and the development of education programs which would be made available to interested licensees and which would explain the VA process and illustrate how to effectively market VA inventoried properties. The VA

Advisory Council would also be responsible for designing the appropriate description format for the information system and keeping it current and uniform.

Aside from the actual marketing plan, further recommendations were made to VA on current program procedure:

- Submit sufficient information on VA-inventoried properties for transfer to local board/state association forms for dissemination to all licensees;

- Adopt a non-discriminatory policy regarding payment of real estate brokerage fees to any qualified purchasers;

- Expedite the VA acceptance/response time in order to be competitive in the marketplace;

- Review the pricing of properties on the market, as necessary; and

- Consider a policy of preoccupancy, based on local jurisdiction.

In our professional opinion, we feel the implementation of the marketing plan will provide easier access to the VA program and its inventoried properties. As such, improved disposition of the inventoried properties may assist with the fund's deficit problems and any future funding changes.

Briefly, I would like to comment on Representative Sundquist's legislation, HR 2801. Although the NATIONAL ASSOCIATION OF REALTORS® does not have specific policy on this bill, it has consistently maintained that the marketplace should dictate property price. Conceptually, the Association would agree with permitting the VA Administrator the flexibility to adjust the VA established property price in instances where the local market has experienced an economic change. Although we understand Representative Sundquist's interest in providing a veteran benefit, we are concerned that this proposal may be detrimental to the VA Revolving Fund, as it would not maximize the true value of the inventoried property.

I want to express my appreciation to the Subcommittee for the opportunity to appear today. At this time, I request that my testimony be submitted for the record and, I would be happy to answer any questions you may have. Thank you.

1125 Fifteenth Street, N.W.
Washington, D.C. 20005
202-861-6500

Mortgage Bankers Association of America

STATEMENT OF

RONNIE J. WYNN

PRESIDENT
COLONIAL MORTGAGE COMPANY
MONTGOMERY, ALABAMA

on behalf
of the

MORTGAGE BANKERS ASSOCIATION OF AMERICA

before the

SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS

of the

COMMITTEE ON VETERANS' AFFAIRS
U.S. HOUSE OF REPRESENTATIVES

Hearings on

The Veterans Administration Home Loan Guaranty Program

September 12, 1985

Mr. Chairman and members of the Committee, my name is Ronnie J. Wynn. I am President of Colonial Mortgage Company of Montgomery, Alabama. I am also Vice Chairman of the Legislative Committee of the Mortgage Bankers Association of America.* Accompanying me are Burton C. Wood, MBA's Legislative Counsel, and Sharon M. Canavan, MBA's Deputy Legislative Counsel. MBA appreciates the opportunity to appear before you today to testify on the Veterans Administration (VA) Home Loan Guaranty Program.

MBA believes that the VA Home Loan Guaranty Program is an excellent one and that the VA has operated the program well. An MBA Task Force has made a number of recommendations designed to lessen program losses by tightening underwriting guidelines, origination methods, appraisal standards, and servicing procedures, as discussed later.

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*The Mortgage Bankers Association of America is a nationwide organization devoted exclusively to the field of mortgage and real estate finance. MBA's membership comprises mortgage originators, mortgage investors, and a variety of industry-related firms. Mortgage banking firms, which make up the largest portion of the total membership, engage directly in originating, financing, selling, and servicing real estate investment portfolios. Members include:

- o Mortgage Banking Companies
- o Mortgage Insurance Companies
- o Life Insurance Companies
- o Commercial Banks
- o Mutual Savings Banks
- o Savings and Loan Associations
- o Mortgage Brokers
- o Title Companies
- o State Housing Agencies
- o Investment Bankers
- o Real Estate Investment Trusts

MBA headquarters is located at 1125 15th Street, N.W., Washington, D.C. 20005; telephone: (202) 861-6500.

MBA also urges that several other amendments be made to the home loan guaranty program. The VA should be authorized to guarantee adjustable rate mortgages (ARMs) with such limits, if any, as the Administrator deems necessary. MBA urges Congress to remove administratively set interest rate ceilings so that interest rates can be freely negotiated between borrower and lender. And, with respect to vendee loans, the Administration should be freed to make the best deal possible when selling properties acquired by the VA in the program. However, setting quotas to increase the number of cases in which the VA refuses to acquire title to property after default is not a favorable adjustment.

OPERATION OF THE VA HOME LOAN GUARANTY PROGRAM

The VA Home Loan Guaranty Program is an entitlement program established under the Serviceman's Readjustment Act of 1944. The program's purpose is to assist qualified veterans to achieve homeownership. The program provides two primary benefits to qualified veterans. First, the VA guarantees a portion of the veteran's mortgage principal. The amount of this guaranty has varied over the years and is now 60 percent of the loan amount, up to a maximum of $27,500. The second benefit offered by the program is the stipulation that no downpayment need be required by the lender. On an annual basis from 1977 to 1984, between 58 percent and 70 percent of VA-guaranteed loans closed were 100 percent no-downpayment loans. (See Exhibit 1.)

Since the VA initiated its program in 1944 until the end of 1984, 11.5 million loans have been guaranteed under the VA Home Loan Guaranty Program. The vast majority of those loans have cost taxpayers only the administrative cost of processing the initial approval. Only 4 percent of those loans have resulted in foreclosure. The foreclosure rate for VA-

guaranteed loans has increased somewhat in the past two years following the severe recession that gripped the U.S. economy and the historically high unemployment rates that resulted (Exhibit 2 and Exhibit 3).

The Loan Guaranty Revolving Fund (LGRF) was established to balance the income and expenses caused by the operation of the program. Income for the fund is derived primarily through the sale of "vendee" loans. Vendee loans are loans made by the VA to a borrower when a VA-acquired property is sold. Expenses accrued by the LGRF are predominantly from the acquisition of foreclosed properties.

Historically, when the LGRF was in a deficit position, the VA transferred money from its Direct Loan Revolving Fund (DLRF). The DLRF exists as a result of a former VA policy to make direct loans in credit-short areas to veterans who could find no other lender to make a VA-guaranteed loan. In such instances, the VA acted as a lender and the earnings on the direct loans provided the VA with a surplus in the DLRF.

Three years ago, the VA was instructed by the Administration to make no more direct loans. Consequently, the net earnings of the DLRF are diminishing. Thus, at a time when the LGRF is experiencing great cash demands due to the recent recession and ensuing increased foreclosures, the DLRF is in its most illiquid position.

A dramatic consequence of the reduction of the DLRF's ability to provide funding for the LGRF has been to make it appear that the loan guaranty program is experiencing losses beyond expectations and greater than comparable mortgage programs. In fact, the change in the VA Home Loan Guaranty Program foreclosure and claim rate actually has been better, relatively, than the increase in foreclosures of conventional loans, which are loans that are not insured or guaranteed by the government (Exhibit 4). And compared with the

FHA, while VA-guaranteed loans have had a higher foreclosure rate than FHA-insured mortgages since the mid 1970s, the relative relationship has remained substantially constant (Exhibit 5). These relative relationships suggest that the VA program is inherently sound and being operated consistent with the mortgage programs of the FHA and conventional lenders.

The only significant aberration that MBA has noted in the recent foreclosure statistics of the VA Home Loan Guaranty program are those for restoration loans. Restoration loans are those guaranteed by the VA pursuant to a restoration of entitlement to a veteran who has paid off (or had another eligible veteran assume) an earlier loan guaranteed by the VA.

While the proportion of VA-guaranteed restoration loans remained substantially constant from 1978 to 1983 at 11 percent of loans guaranteed, the proportion of claims for restoration loans has risen steadily from 1.3 percent of total claims to 7.9 percent from 1978 to 1984 (Exhibit 6 and Exhibit 7). The information available does not yet provide an explanation of this disproportionate increase, but further study is suggested.

FY 1986 BUDGET PROPOSALS: USER FEE INCREASES

I would like to thank the Chairman and the Subcommittee members for your support in rejecting any increase in the VA origination fee as proposed by the Administration. Your opposition to such an increase was most helpful in defeating that proposal during consideration of the FY 1986 budget resolution.

It may well be that new taxes will be necessary to allow the Government to reduce the Federal budget deficit, but those taxes should be broad-based and should be decided upon

in an open discussion of tax policy. The 5 percent user fee proposal constituted a back-door levy on homebuying veterans, thinly disguised as a cost-related user fee intended to strengthen the program.

In proposing that homebuying veterans should increase their mortgage debt by the amount of the proposed additional origination fee, the Administration was asking veterans to shoulder the burden of expenses brought about by other veterans who entered the home loan guaranty program earlier. This is another reflection that the proposed fee was not user-cost related. Moreover, it shows a willingness of the Administration to transfer the burden of general government obligations, entered into willingly in the past, to a specific, targeted group of taxpayers who are not specifically benefitting from those obligations.

When Congress created the VA Home Loan Guaranty Program in 1944 to assist veterans returning from World War II to buy a home, Congress did not design it or intend it to be user-fee supported. The program was a recognition by a grateful nation that the men and women who had forgone civilian life, many of them against their will, to defend the vital interests of the country should be aided in achieving a home. The program was partial payment for services performed.

From the beginning, there was a realization that the program would need appropriations, and appropriations have been made in several fiscal years during the operation of the program. In 1984, Congress was faced with the fact that the economic cycle and certain changes in other VA operations precluded the VA from funding the home loan guaranty program from internal VA sources, and that appropriations would be required to continue the program.

Last year, Congress considered whether to renew its commitment to qualified veterans, especially the Vietnam veterans who are now reaching the point in their lives when they are ready to buy a home. The requested authorization and appropriations were granted, the VA was directed to administer the program in certain ways to reduce costs, and a 1 percent temporary funding fee that would expire September 30, 1987 was imposed.

The effects on the program of the 1984 directives by Congress, of course, need to be studied, and the program may need further adjustments. But as recently as a year ago, Congress renewed its commitment to qualified veterans to assist them in buying a home.

MBA REPORT OF THE VA TASK FORCE

At the suggestion of VA Administrator Harry Walters, MBA appointed a VA Task Force of industry experts. Last week MBA received the VA response to the MBA Task Force Report. As soon as that response is evaluated, MBA will forward its response to this Subcommittee for inclusion in the hearing record.

The MBA Task Force Report provided for the following recommendations:

Origination and Underwriting Standards

Many defaults can be tied to lax origination and underwriting standards. While the intent of the VA Home Loan Guaranty Program is to expand the mortgage credit opportunities of veterans, it is a disservice to a borrower to extend credit where the borrower's default may be likely.

VA should reevaluate its home loan guaranty program procedures with an eye toward designing procedures that assure that only creditworthy veterans are recipients.

VA's underwriting guidelines as to the financial capabilities of the borrower are less stringent than those of the conventional mortgage market and the Federal Housing Administration (FHA). For example, for fixed-rate loans the conventional mortgage market relies on a housing expense ratio not to exceed 25 to 28 percent of an applicant's gross monthly income and a debt-to-income ratio not to exceed 30 to 36 percent of an applicant's gross monthly income. FHA uses a housing expense ratio not to exceed 35 percent of an applicant's net effective income (a proposed change will make this 38 percent) and a debt-to-income ratio not to exceed 50 percent of an applicant's net effective income (a proposed change will make this 53 percent). VA uses no such system of maximum allowable debt and/or housing expense ratios.

Instead of establishing maximum ratios for housing expenses and debts, VA offices rely on the residual method of underwriting; that is, the amount of monthly income a family should have left after meeting housing and debt obligations. Each VA locality establishes a minimum income residual for differing family sizes based on a survey of local factors. The residual income levels are guidelines for underwriting, and each veteran's loan application is reviewed from a total underwriting standpoint, taking into consideration all applicable factors that indicate the veteran's capacity and probability of repaying the loan. Nevertheless, underwriters rely on the residual income amount as the key factor in approving the loan. The conventional market does not use residuals at all, and FHA uses residuals to a limited degree in addition to ratios.

In light of the current losses in the VA program, it is time that VA reexamine its underwriting criteria toward relying less on the residual approach and designing underwriting criteria that rely to a greater degree on debt and housing expense analysis.

An increase in standards for future VA home loan originations will not serve to minimize losses on loans already made that may end in foreclosure. A positive effect will not be felt immediately but would result in the long run.

VA lenders should consider stiffening their individual companies' underwriting guidelines for VA loans beyond those imposed by VA.

Only the VA can institute stringent, comprehensive underwriting standards for the VA Home Loan Guaranty Program. VA should immediately undertake a reexamination of its approval standards. In the meantime, VA lenders should realize that there is need for more stringent underwriting guidelines for VA loans. VA lenders should consider stiffening their individual companies' underwriting guidelines for VA loans beyond those imposed by VA originations. These increased standards should include both better underwriting of appraisals and more stringent consumer credit underwriting.

VA loan field offices should be instructed that loan underwriting decisions should be made exclusive of "pressure" imposed on that office by veteran applicants and/or real estate sales agents.

When loans are being processed by VA field offices, veteran applicants and/or real estate sales agents often contact the field office staff to find out the status of the loan application and often to pressure the staff into approving the loan. Status calls should be restricted to the VA lender submitting the loan application on behalf of the veteran

applicant. Veterans may not submit applications directly to VA but must use a VA approved lender. VA field offices are particularly sympathetic to pressure received directly by the veteran applicant for loan approval.

VA loan guaranty field office staff are guided by the premise that they should do everything possible to get the veteran into the house that the veteran has selected to purchase. The result of this attitude is that some veterans who were never really qualified to purchase a home were approved for VA home loans. Often the result is foreclosure. Today's mortgage market is one with little or no inflation, which means that veterans faced with foreclosure often are in a situation where the house has not appreciated in value and actually may be worth less than it was at the time of purchase. In the event of claim, VA must pay on behalf of the veteran.

Restricting the veteran's direct access to the VA field loan approval officer will limit the pressure being placed on the VA directly by the veteran to approve the loan. The VA approved lender, submitting the application on behalf of the veteran applicant, should be responsible for contacting VA and providing necessary information.

VA should encourage VA lenders to increase the use of the VA Automatic Program.

Delinquency and foreclosure rates under the VA Automatic Program are consistently less than these rates under the VA prior approval program. Lenders using the VA Automatic Program report that underwriting criteria, particularly credit underwriting procedures, used by their companies in underwriting "Automatic" loans are more stringent than those required by VA. These increased underwriting criteria are among the reasons cited for the lower foreclosure rates associated with the VA Automatic Program.

VA can encourage the use of the VA Automatic Program by publicizing the availability of the program to lenders not using the program and by emphasizing the benefit of faster processing time available under the program. Real estate agents and builders can be provided with lists of lenders who are approved under the Automatic Program.

Since VA prior approval delinquency and foreclosure rates are higher than those under the Automatic Program, it is often stated that Automatic Lenders often take the easier underwriting decisions and leave the "tough calls" to VA. Increased use of the Automatic Program should mean the industry will apply its more stringent underwriting criteria to these "tough calls" and will probably result in less of these loans being made. This could have a positive effect on delinquency and foreclosure rates.

VA should develop a system that identifies a loan that is resubmitted to VA on a prior approval basis or resubmitted to another VA Automatic Lender when it was rejected by a lender using the Automatic Program.

VA lenders using the Automatic Program report many instances where they reject a VA loan but the veteran subsequently resubmits the loan to another VA Automatic Lender who approves the loan or submits the loan to VA on a prior approval basis. Sometimes the lender who has rejected the application under the Automatic Progam is "pressured" into resubmitting the loan to the VA for approval under the prior approval program. There is no system in place that identifies a loan application as having been rejected by another lender or as having been rejected under the Automatic Program by the submitting lender or any other Automatic Lender. VA Automatic Lenders and VA should know if the loan application was previously rejected and should consider such a rejection when underwriting the loan.

VA lenders should determine if their companies are sending rejected VA automatic loans through VA on a prior approval basis.

Loans that are rejected under the Automatic Program are sometimes resubmitted to VA by a company's branch offices under the prior approval program. Often these loans end up being approved by VA. As previously discussed, VA does not have a system in place that identifies a loan as having been rejected by an Automatic Lender. VA lenders, as part of their internal quality control procedures, should determine if their companies are sending rejected VA Automatic loans through VA on a prior approval basis, and if so, instructions should be given to underwriters and loan origination personnel to stop such actions in order to achieve higher quality underwriting of all VA loans.

Appraisals

Quality appraisal methods are another area of concern. With the current trend of stabilization and even deflation in housing prices, lenders can no longer rely on inflation to "bail out" bad appraisal decisions. Therefore, high-quality appraisal techniques must be developed, and lenders should carefully scrutinize appraisals when underwriting a loan application.

Lenders' underwriters should develop expertise in appriasal underwriting.

As a result of a request made by the MBA VA Task Force, VA now supplies the full appraisal report, not just the Certificate of Reasonable Value (CRV), to VA lenders. This will provide VA lenders with an opportunity to underwrite the appraisal as a standard part of the origination process of VA loans. In the past VA lenders received only the CRV,

which stated a maximum loan amount but provided no additional information as to the condition of the property or how the value was reached.

As the number of foreclosed VA loans on which the VA chooses to pay the claim and leave the property with the VA lender increases (it is now approaching 14 percent of all VA foreclosures), lenders have found that the appraised value of such homes is often significantly lower than the original appraisal. In many instances these differences in values are due to reductions in property values in the geographic area due to adverse economic conditions. Improved underwriting of appraisals will have little impact in such instances. However, in other instances the difference in values is due to the poor quality of original appraisals.

Underwriters need to make use of information provided in the appraisal report to determine the adequacy and accuracy of the appraisal. VA lenders need to train their underwriting personnel in appraisal review skills so that when appropriate, underwriters can question appraisers on the appraisal report and factor in questions on the value of the property in the underwriting decision. Adjustments to appraised values should be made where appropriate.

VA lenders should also develop procedures for reordering an additional appraisal if their underwriter's review uncovers considerable problems with the appraisal as submitted by the VA assigned appraiser.

A standard appraisal form should be developed for use by VA, FHA, FNMA, and FHLMC.

Currently the VA and FHA use one appraisal form and the Federal National Mortgage Association (FNMA) and the Federal Home Loan Mortgage Corporation (FHLMC) use

another. The conventional appraisal form provides more information than the FHA/VA form. VA, FHA, FNMA, and FHLMC officials, along with representatives of appraisal organizations, are meeting on a regular basis to design a single appraisal form to be used by all of these organizations. The uniformity of one form and the availability of an increased amount of information to be used by underwriters in evaluating appraisals will have a positive effect on the quality of appriasals.

VA should consider allowing lenders to select appraisers.

Currently VA establishes the criteria for putting appraisers on its panels, and VA local field offices assign appraisers. VA lenders are not allowed to select appraisers that are to be used for their applications.

VA officials have consistently maintained that they are opposed to allowing VA lenders to select appraisers because lenders are inclined to pressure appraisers to come in with a higher value than appropriate for the property. Appraisers tend to respond to such pressure, VA claims, because they want to continue working for a particular lender. Certainly there is some justification for this concern. However, the existence and importance of lenders' quality control systems are greater than ever because of today's deflationary economy. Lenders already establish criteria and hire appraisers for conventional loans. Adjustments in appraised values occur frequently on conventional loans because of quality control systems that are in place. Appraisers being used by lenders for their conventional loans are often removed from a particular company's list of approved appraisers because of poor quality appraisals.

At a minimum, VA should produce a list of its approved appraisers and allow lenders to select from that list. Another alternative would be for VA lenders to be able to veto a particular appraiser that VA assigns to a case if the lender has evidence of consistently

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poor quality appraisals from that particular appraiser. VA needs to be more conscientious in reviewing the quality of its approved appraisers and removing appraisers who consistently submit poor quality work.

Servicing and Foreclosure

VA should exclude from indebtedness the amount of interest that accrues during periods of forbearance. This should include bankruptcy workouts.

When a forebearance agreement is in place with a veteran borrower, VA should "stop the clock" on interest due to VA that is being accumulated during this forbearance agreement. In the case of bankruptcy workouts, this "stop the clock" procedure for interest accumulation should also be imposed.

VA should encourage lenders to contract with third-party counselors for the purpose of making pay-out arrangements with delinquent borrowers.

Third-party counseling services are available for hire. Some lenders have successfully used such services for conventional loans in danger of being foreclosed. These third-party counselors work on a commission basis and are not employees of VA lenders. VA lenders can enter into contractual agreements with these third-party counselors to work out payment arrangements with delinquent borrowers. Typically these counselors will use creative approaches, such as leasing back the property to the borrowers and giving the borrower an opportunity to repurchase the property at a future time. The use of such third-party counselors should be a pre-foreclosure accommodation encouraged by VA, as it could have the effect of costing VA less than paying out the guaranty.

VA should encourage the use of reputable third-party counselors by notifying VA lenders of their availability.

VA lenders should review VA foreclosed loans to determine the major problem areas creating losses so that VA can use this information in redesigning its underwriting criteria.

As part of their quality control system, VA lenders should review all foreclosed VA loans to determine the major problem areas where losses recur. As a particular deficiency is uncovered, a company's underwriting criteria should be revised to reflect and solve the deficiency. For example, some VA lenders have reported that VA losses repeatedly come from borrowers who had a bad credit history. Another problem repeatedly identified in foreclosed VA loans is the veteran borrower with no cash left after settlement. As VA lenders identify such problem areas, they should institute more stringent underwriting criteria.

VA lenders need to be aware that in the event of foreclosure, if the house is abandoned and vacant, lenders can proceed with foreclosure without approval from the VA field office.

VA officials have indicated that in the event that a foreclosed house is abandoned and vacant, lenders can proceed with foreclosure without approval from the VA field office.

VA lenders should make use of the procedure allowing VA to pay a partial claim in those instances where someone can take over the property for less than is due.

VA officials have indicated that VA will pay a partial claim in those instances where someone can take over the property for less than is due. The original veteran is always held liable for any claim that VA pays on his or her behalf.

VA lenders should make use of the procedure that allows veterans to be paid for a deed in lieu of foreclosure as long as VA approves the deed in lieu.

VA officials have indicated that veterans can be paid for a deed in lieu of foreclosure as long as the VA approves the deed in lieu. Such a procedure allows lenders to process claims more quickly. VA's primary consideration in approving this procedure is whether the veteran is able to pay the debt. VA will approve a deed in lieu only if the veteran borrower is unable to pay the debt, because acceptance of such deeds precludes a VA claim against the veteran for amounts paid under the guaranty. VA local field offices have authority to make these approvals.

VA field offices should issue bidding instructions on foreclosed properties on a timely basis.

A serious and recurring problem is that many lenders have had to postpone foreclosure sales repeatedly because they did not receive timely bidding instructions from the VA field offices. The VA has had problems obtaining and evaluating property appraisals in time to issue upset prices for scheduled sales.

Postponement of a foreclosure sale is very costly to the VA and the lender. It unnecessarily extends the time needed to accomplish the liquidation and increases the debt. The VA should take the necessary action to ensure that bidding instructions are received by lenders prior to the scheduled sale date.

VA DISCOUNTED SALES PROGRAM: HR 2801

HR 2801 would authorize VA to establish a program where VA-held properties would be sold at a discount of 80 percent after three months, 75 percent after seven months, and 70 percent after one year.

MBA is concerned that such a program would lead to even greater losses in the Loan Guaranty Revolving Fund (LGRF). This would further fuel the effort to impose larger user fees on veteran borrowers and higher losses to the LGRF could result in VA requiring lenders to take back even more properties.

Part of MBA's concern with this proposal is that the automatic price reduction would simply prompt potential buyers not to bid on properties until properties were discounted. So long as interest rates are at affordable levels, properties should sell within a reasonable time period if fairly priced.

In order to move its inventory, VA should place more emphasis on pricing homes at their market value. Rather than an automatic sales price discount, VA should review its assigned price after a certain time period. VA should look at comparable sales prices or even order an updated appraisal to confirm that the assigned price is a fair market value.

VA needs flexibility in order to respond to local market conditions. Some markets are stable, while in othes prices are stagnant or deflating. VA's pricing should take these variances into account and VA pricing procedures should continue to be flexible so that prices can be re-analyzed, if necessary.

VA's recent change requiring lenders to take back properties in many cases has allowed VA, to a great extent, the luxury of taking back title to the "best" properties. Presumably, these are the homes most likely to be readily saleable. Therefore, MBA opposes any automatic discount schedule in order to minimize losses to the LGRF.

VA PAYMENT OF CLAIMS

In its FY 1985 Budget proposal, the Administration proposed that the VA should pay in full the claims under the VA home loan guaranty program, and leave with the lender the responsibility of disposing of the property securing the guaranteed loan. This recommendation, while rejected by Congress, has not been acknowledged as abandoned by the Administration, and so, must be addressed. The recommendation apparently rested on the assumption that, if the VA ceases to acquire foreclosed properties, there will be an enormous apparent cost savings to the government.

The VA will not save money by paying the lender the guaranty amount in all foreclosure cases. When the past experience of the VA is examined, it is clear that, since 1979, the average loss on properties acquired and subsequently sold is about $10,000 less than if the VA had paid the average guaranty on those properties (Exhibit 8).

Effect on Lenders and Veterans

The change in the VA guaranty settlement policy not yet abandoned by the Administration affects both VA lenders and veterans themselves.

As a group, mortgage bankers make about three-quarters of all VA-guaranteed loans, more than any other category of lenders (Exhibit 9). Thus, mortgage bankers would be affected more than other lenders by the change in VA policy. The impact will affect certain aspects of a lender's business, as well as the lender's perception of the risk potential of a VA-guaranteed loan.

One of the major assumptions made by the Administration is that, if the VA does not acquire a property by entering a bid to do so, there will be a third party who will acquire the property from the lender. This assumption sidesteps the issue of a lender being left holding title to property. The assumption that a third party buyer would come forward assumes a perfect market. There may be a prospective buyer in the market for the foreclosed property at a price near or below what the VA would have bid. The problem is that foreclosure sales require ready cash and information not available to most buyers.

A more realistic scenario is that, if the VA enters no bid, in only a small percentage of cases will a third party take title to the property. The majority of foreclosures will result in the lender taking title to the property and being responsible for maintenance, renovation, marketing, and eventual sale of the property.

The vast majority of lenders, especially small mortgage bankers, are not capitalized to deal with property disposition. In order to complete the transfer quickly and efficiently, lenders would be forced either to develop property disposition centers or turn to others

who, for a fee, would handle the property disposition. Either approach would put lenders, especially the smaller ones, under great financial strain. Needless to say, it would also make VA-guaranteed loans less attractive to lenders and increase the cost of mortgage credit to veteran borrowers.

VA-guaranteed loans would likely be perceived as carrying a much larger share of risk to lenders in the mortgage markets. Lenders would then begin to apply more stringent underwriting procedures to applications of prospective VA borrowers, and a higher yield would be required in the market to compensate investors for the additional risk they are accepting by purchasing a VA-guaranteed loan.

VENDEE LOANS

The President's budget for FY 1985 indicated that the VA would discontinue selling vendee loans with recourse. MBA opposed that proposed change in current practice. Sale of vendee loans without recourse shifts the credit risk of default from the VA to private purchasers, and purchasers necessarily adjust their purchase prices accordingly. Because of its size, and because it is the lender, the Government is a more efficient manager of vendee loan credit risk than any private buyer can be. Therefore, it can be expected that the reduction in the sales price paid by the private industry buyers of vendee loans will be greater than the savings the Government might realize by transferring the risk of default. In the Deficit Reduction Act of 1984 (PL 98-369), a target of the proportion of vendee loans was set for the VA. MBA urges that the quota concept be removed, and that the VA be allowed to use guaranteed vendee loans as fully as it deems economically advantageous in selling property acquired in the home loan guaranty program.

INCREASE IN GUARANTY MAXIMUM

MBA supports the proposal included in S 9, a bill introduced by Senator Robert Byrd on behalf of Senator Alan Cranston, to increase the maximum amount of the VA loan guaranty from $27,500 to $35,000 for home loans and from $20,000 to $22,000 for manufactured housing loans. Such an increase would bring the relationship between the level of the guaranty amount and the ever increasing cost of new and existing housing closer to historical ratios.

From 1974 to 1984, the median price of new single-family homes sold jumped from $35,900 to $79,900, an increase of 123 percent. Had the VA maximum guaranty been adjusted annually in equal proportion to the increase in new home prices, the 1984 guaranty would have reached $39,000.

The median price of existing single-family homes sold increased over 120 percent during the period 1974 through 1984, from $32,000 in 1974 to $72,800 in 1984. Adjusting the VA maximum guaranty for annual increases in existing home prices for this period would have resulted in a maximum guaranty of over $39,800 in 1984 (Exhibit 10 and Exhibit 11).

FREE VA INTEREST RATE

Under current law, the maximum interest rate allowable on a mortgage guaranteed by the VA is fixed by the VA Administrator. MBA has consistently urged that the law be amended to allow interest rates to be determined by the market.

ADJUSTABLE RATE MORTGAGES

MBA urges that the VA be authorized to include adjustable rate mortgages (ARMs) in the home loan guaranty program. During the past three years, ARMs have become accepted by borrowers in the conventional mortgage market. FHA has expanded its insurance program to include ARMs. These markets have demonstrated that ARMs are a beneficial development that permits borrowers and lenders to tailor transactions to the needs of borrowers. Borrowers who do not want to pay for the predictability of a fixed rate mortgage can achieve the lower interest rates that lenders can offer when the borrower bears some of the risk of inflation or other economic conditions that cause rates generally to rise.

In his bill, S 9, Senator Cranston has proposed authorizing the VA to guarantee ARMs. To the extent that the measure would accomplish this purpose, MBA supports the bill. However, S 9 would limit the ability of borrowers and lenders to reach the best arrangement between them, because adjustments in interest rates provided in VA guaranteed mortgages would be subject to four limits or "caps" enumerated in the bill.

MBA is opposed to statutory caps on ARMs. Adjustments should be freely negotiated, just as traditional long-term fixed rate mortgage interest rates should be. At the most, authority could be left with the Administrator of the VA to set caps for ARMs in the home loan program as the program and the veterans it benefits gain experience with ARMs.

Experience with the FHA-ARM insurance program caps of 1 percent per annum increase, which would be placed on VA ARMs by S 9, is that investors in the market are not attracted. HR 1, as reported out by the Banking Committee, would increase this cap from 1 percent to 2 percent.

Whatever may have been the case previously, ARMs are no longer an untested and unknown quantity. Approximately 53 percent of new conventional mortgages originated in the last quarter of 1983 were ARMs, and the percentage has risen to 57 percent by the last quarter of 1984. (Federal Home Loan Bank Board "Conventional Home Mortgage Rates," February 4, 1985.)

We appreciate the opportunity to appear before the Committee, and we would be pleased to furnish any additional information that may be needed.

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 1

VA HOME LOAN GUARANTY PROGRAM ACTIVITY
PRIMARY HOME LOANS CLOSED

Total [1]/

	Number	Loan Amount ($Mil)	Average Loan Amount	Average Purchase Price	Avg. Loan to Value Ratio
1977	371,610	13,260	$35,683	$36,982	96.5
1978	352,797	13,959	$39,567	$41,079	96.3
1979	345,708	15,991	$46,256	$48,555	95.3
1980	255,631	13,257	$51,860	$55,092	94.1
1981	136,027	7,543	$55,452	$58,833	94.3
1982	87,027	5,053	$58,062	$63,112	92.0
1983	227,155	14,092	$62,037	$66,723	93.0
1984	181,771	11,633	$63,998	$67,584	94.7

[1]/Loans for refinancing not included.

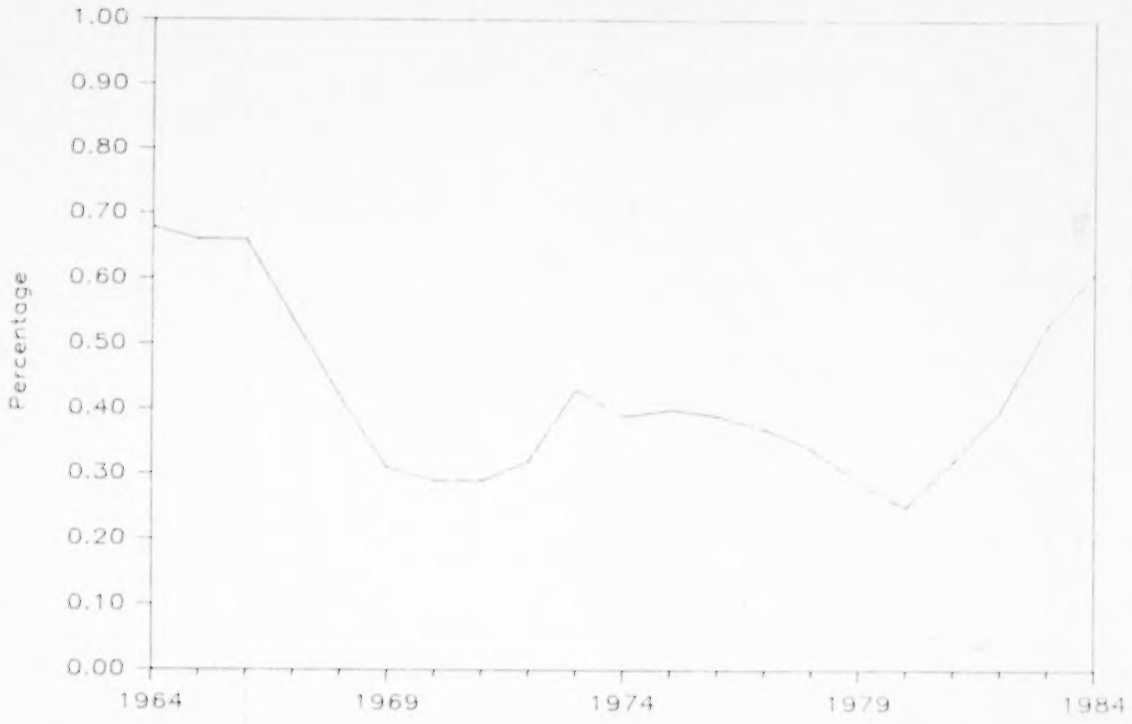
100% Loans

	Number	Percent of Total Number	Loan Amount ($Mil)	Average Loan Amount
1977	259,509	69.83	8,817	$33,975
1978	244,458	69.29	9,091	$37,188
1979	234,810	67.92	10,260	$43,695
1980	169,839	66.44	8,195	$48,254
1981	89,758	65.99	4,569	$50,901
1982	50,285	57.78	2,629	$52,284
1983	137,315	60.45	7,868	$57,299
1984	118,218	65.04	7,042	$59,564

Source: Program Management Service, Loan Guaranty Department of the Veterans Administration.

Prepared by Mortgage Bankers Association of America, Economics Department, September 1985.

VA CLAIMS PAID DURING YEAR AS A PERCENT OF VA LOANS OUTSTANDING END OF YEAR



Source: Veterans Administration, Loan Guaranty Department

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 3

FORECLOSURES STARTED
(Percent of Number of Loans Serviced)

	VA	FHA	CONVENTIONAL
1979	.70	.78	.25
1980	.71	.74	.31
1981	.72	.82	.41
1982	.92	1.07	.53
1983	.97	1.04	.62
1984	.95	1.03	.62

Source: National Delinquency Survey, Mortgage Bankers Association of America, February 1985.

FORECLOSURES COMPLETED
(Percent of Number of Loans Outstanding)

	VA 1/	FHA 2/	CONVENTIONAL 3/
1979	.30	.48	.09
1980	.25	.41	.12
1981	.32	.40	.18
1982	.40	.46	.33
1983	.53	.67	.40
1984	.61	.75	.37

Sources:
1/ Veterans Administration
2/ Federal Housing Administration
3/ Federal Home Loan Bank Board. Note: Includes all conventional mortgage loans.

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985.

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 4

NUMBER OF FORECLOSURES STARTED DURING QUARTER AS A PERCENT OF NUMBER OF LOANS SERVICED FOR 1- TO 4-UNIT RESIDENTIAL MORTGAGE LOANS

Yr. Qtr.	VA	FHA	Conv.
1973.1	0.18	0.43	0.05
1973.2	0.19	0.41	0.05
1973.3	0.19	0.40	0.06
1973.4	0.18	0.40	0.07
1974.1	0.18	0.37	0.08
1974.2	0.17	0.38	0.06
1974.3	0.19	0.37	0.08
1974.4	0.20	0.38	0.09
1975.1	0.21	0.33	0.10
1975.2	0.23	0.34	0.10
1975.3	0.21	0.31	0.09
1975.4	0.19	0.26	0.09
1976.1	0.18	0.24	0.07
1976.2	0.19	0.20	0.08
1976.3	0.19	0.21	0.08
1976.4	0.20	0.24	0.09
1977.1	0.22	0.24	0.08
1977.2	0.21	0.23	0.08
1977.3	0.20	0.22	0.07
1977.4	0.19	0.20	0.07
1978.1	0.19	0.21	0.06
1978.2	0.18	0.22	0.06
1978.3	0.20	0.21	0.06
1978.4	0.20	0.22	0.07
1979.1	0.19	0.22	0.07
1979.2	0.17	0.19	0.06
1979.3	0.15	0.16	0.06
1979.4	0.19	0.21	0.06
1980.1	0.16	0.16	0.07
1980.2	0.17	0.18	0.07
1980.3	0.19	0.20	0.08
1980.4	0.19	0.20	0.09
1981.1	0.18	0.20	0.09
1981.2	0.19	0.22	0.11
1981.3	0.16	0.19	0.10
1981.4	0.19	0.21	0.11
1982.1	0.22	0.26	0.13
1982.2	0.22	0.24	0.13
1982.3	0.24	0.28	0.13
1982.4	0.24	0.29	0.14
1983.1	0.23	0.26	0.14
1983.2	0.26	0.28	0.16
1983.3	0.24	0.26	0.15
1983.4	0.24	0.24	0.17
1984.1	0.23	0.23	0.13
1984.2	0.24	0.25	0.16
1984.3	0.27	0.30	0.18
1984.4	0.21	0.25	0.15
1985.1	0.27	0.30	0.17

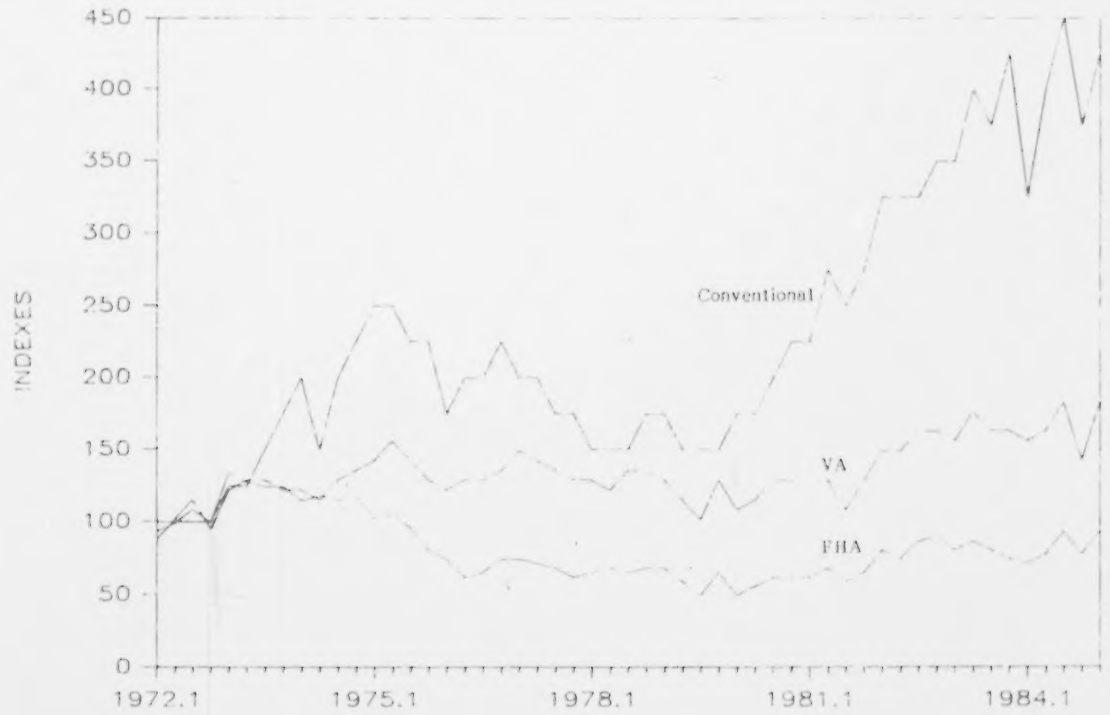
Source: National Delinquency Survey, Mortgage Bankers Association of America.

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985.

EXHIBIT 5

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

GROWTH IN FORECLOSURES STARTED
INDEXES (1972 = 100)



Source: National Delinquency Survey, Mortgage Bankers Association of America

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 6

VA RESTORATION USE AND FORECLOSURES

	Restoration Use (Percent of Originations)	Restorations Foreclosures (Percent of All VA Foreclosures)
1978	10.3	1.3
1979	11.0	1.6
1980	11.2	2.9
1981	10.4	4.4
1982	10.1	6.6
1983	10.6	7.7
1984	10.8	7.9

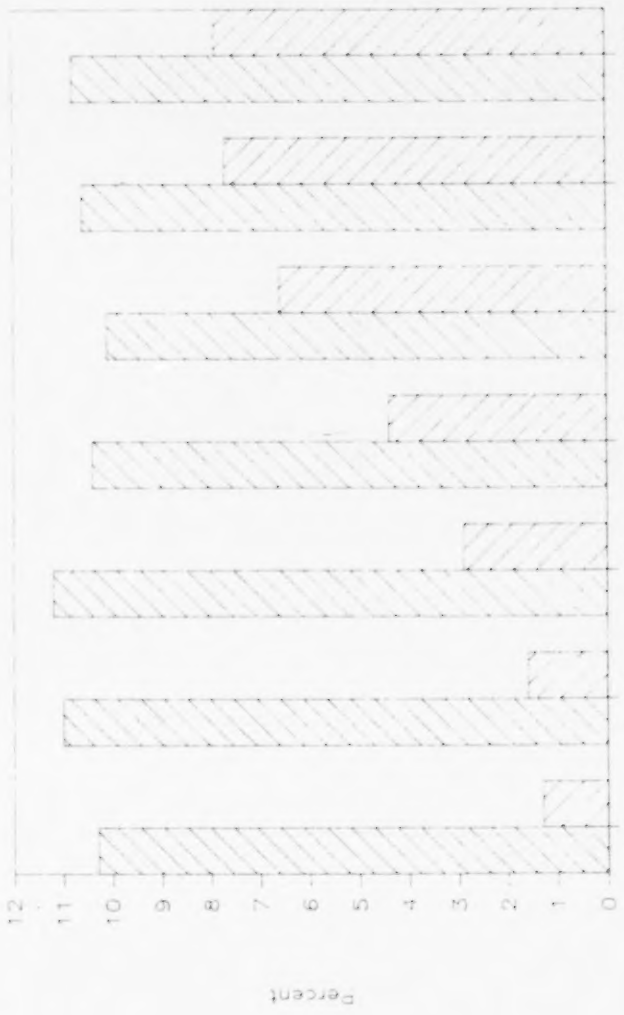
Source: Veterans Administration, Loan Guaranty Department

Prepared by the MBA Economics Department, September 1985.

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 7

VA RESTORATION USE AS A PERCENT OF VA ORIGINATIONS, AND
RESTORATIONS FORECLOSED AS A PERCENT OF ALL VA FORECLOSURES

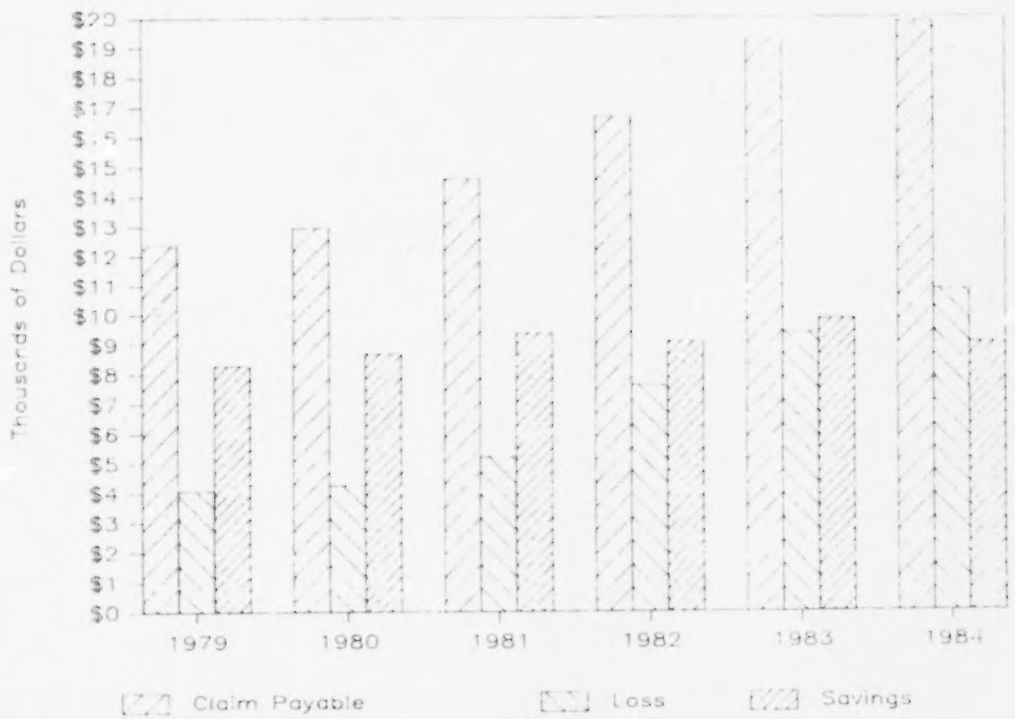


Source: Veterans Administration, Loan Guaranty Department
Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 8

AVERAGE VA CLAIM PAYABLE FOR PROPERTY SOLD DURING FISCAL YEAR;
AVERAGE LOSS FOR PROPERTY SOLD DURING FISCAL YEAR;
AVERAGE SAVINGS FROM SALE OF PROPERTY DURING FISCAL YEAR



Source: Veterans Administration, Loan Guaranty Department

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 9

MORTGAGE BANKERS ORIGINATIONS OF VA AND FHA RESIDENTIAL LOANS AS A PERCENT OF TOTAL VA AND FHA RESIDENTIAL ORIGINATIONS

	Mortgage Bankers Originations ($ millions)		Percent of Total Originations of:	
	VA	FHA	VA	FHA
1975	$ 6,326	$ 4,601	71.6%	73.4%
1976	7,381	5,096	70.8	72.8
1977	11,624	8,228	78.1	78.6
1978	12,372	11,587	77.2	79.5
1979	15,554	17,397	82.4	83.9
1980	9,567	12,161	79.1	81.3
1981	6,044	8,736	80.2	82.9
1982	6,158	9,808	80.1	85.4
1983	14,148	22,936	74.9	79.8
1984	8,553	12,532	70.7	76.7

Source: Survey of Mortgage Lending, Department of Housing and Urban Development.

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985.

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

	Maximum VA Guaranty		Median Sales Prices					
			Existing Homes		New Homes		All Homes 1/	
	Amount	% Change From 1974	Price	% Change From 1974	Price	% Change From 1974	Price	% Change From 1974
1974	$17,500	NA	$32,000	NA	$35,900	NA	$32,725	NA
1975	$17,500	0.0	$35,300	10.3	$39,300	9.5	$36,026	10.1
1976	$17,500	0.0	$38,100	19.1	$44,200	23.1	$39,162	19.7
1977	$17,500	0.0	$42,900	34.1	$48,800	35.9	$43,981	34.4
1978	$25,000	42.9	$48,700	52.2	$55,700	55.2	$49,891	52.5
1979	$25,000	42.9	$55,700	74.1	$62,900	75.2	$56,825	73.6
1980	$27,500	57.1	$62,200	94.4	$64,600	79.9	$62,572	91.2
1981	$27,500	57.1	$66,400	107.5	$68,900	91.9	$66,782	104.1
1982	$27,500	57.1	$67,800	111.9	$69,300	93.0	$68,057	108.0
1983	$27,500	57.1	$70,300	119.7	$75,300	109.7	$71,232	117.7
1984	$27,500	57.1	$72,800	127.5	$79,900	122.6	$74,094	126.4

		Price Adjusted VA Guaranty			RATIO: Price Adjusted Guaranty to Actual Guaranty		
	Maximum VA Guaranty	For Existing Homes	For New Homes	For All 1/ Homes	For Existing Homes	For New Homes	For All 1/ Homes
1974	$17,500	$17,500	$17,500	$17,500	1.00	1.00	1.00
1975	$17,500	$19,305	$19,157	$19,265	1.10	1.09	1.10
1976	$17,500	$20,836	$21,546	$20,942	1.19	1.23	1.20
1977	$17,500	$23,461	$23,788	$23,519	1.34	1.36	1.34
1978	$25,000	$26,633	$27,152	$26,679	1.07	1.09	1.07
1979	$25,000	$30,461	$30,662	$30,388	1.22	1.23	1.22
1980	$27,500	$34,016	$31,490	$33,461	1.24	1.15	1.22
1981	$27,500	$36,313	$33,586	$35,712	1.32	1.22	1.30
1982	$27,500	$37,078	$33,781	$36,394	1.35	1.23	1.32
1983	$27,500	$38,445	$36,706	$38,092	1.40	1.33	1.39
1984	$27,500	$39,813	$38,948	$39,622	1.45	1.42	1.44

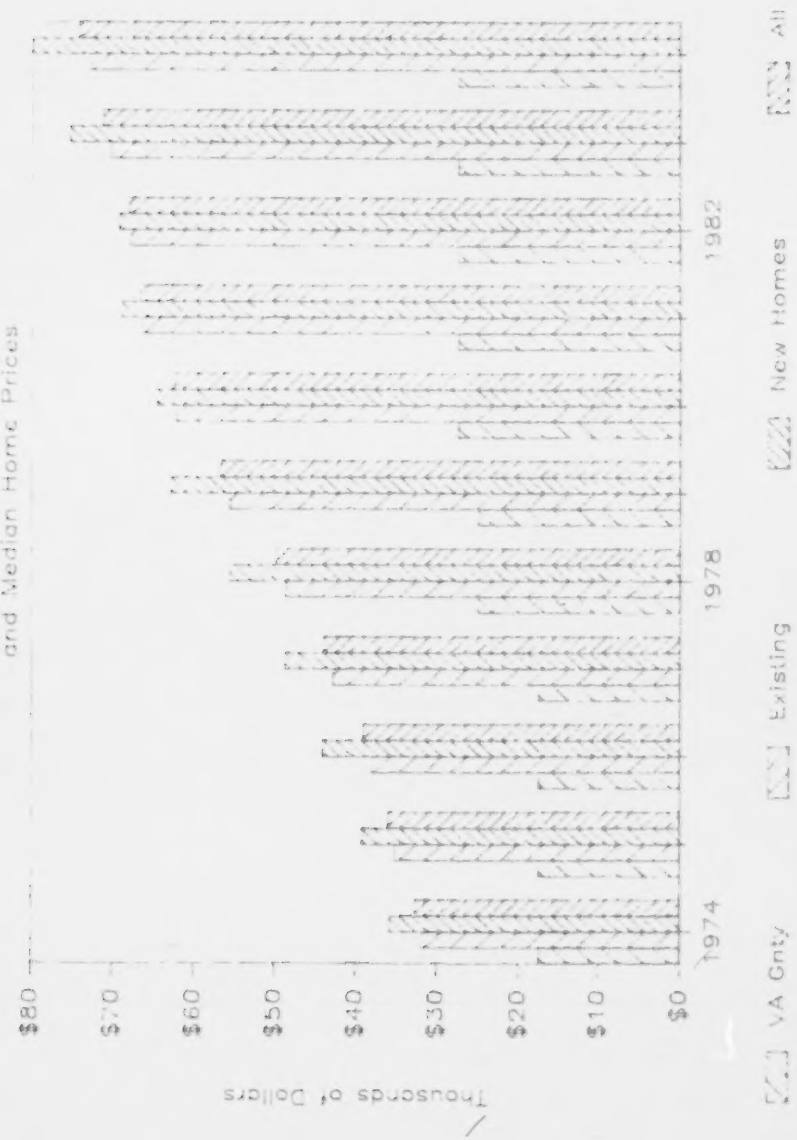
Sources: Bureau of the Census; National Association of Realtors.

1/ Weighted average (by sales activity) of median sales prices of new and existing single-family homes sold.

Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985.

Table to Accompany Statement of Ronnie J. Wynn
Mortgage Bankers Association of America, September 1985

EXHIBIT 11



Sources: Veterans Administration; Bureau of the Census; National Association of Realtors
Prepared by the Mortgage Bankers Association of America, Economics Department, September 1985

Vietnam Veterans of America, Inc
2001 S St NW
Suite 700
Washington, DC 20009-1125

(202) 332-2700

STATEMENT OF

RICHARD F. WEIDMAN

DIRECTOR OF GOVERNMENT AFFAIRS

VIETNAM VETERANS OF AMERICA

Accompanied by

DANIEL F. HAYES, Esq.
SPECIAL COUNSEL

SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS

COMMITTEE ON VETERANS AFFAIRS

UNITED STATES HOUSE OF REPRESENTATIVES

September 12, 1985

Mr. Chairman, my name is Richard Weidman, and I am Director of Government Relations of Vietnam Veterans of America (VVA). Appearing here with me is Mr. Daniel F. Hayes, Special Counsel to Vietnam Veterans of America. VVA thanks you for the opportunity to appear here before this Subcommittee to express our views on aspects of the Veterans' Amdinistration's Home Loan Mortgage Guaranty Program.

I. DISCOUNTED SALES MAKE BUSINESS SENSE

Our statement addresses three areas under the purview of this subcommittee, Mr. Chairman. First, we state our position in favor of HR 2801, and reasons why. Secondly, VVA urges you to consider a GAO investigation into veteran defaults and foreclosures. Third, VVA wishes to inform this body in regard to our knowledge of frauds perpetrated in the manufactured home industry, what Vietnam Veterans of America is doing to seek redress for the veterans so victimizied, and our thoughts on what this body might consider to ensure integrity of this program in the future.

In regard to HR 2801, "To amend title 38, United States Code, for the purpose of establishing a discounted sales program of homes held by the Veterans' Administration for an extended period of time, Vietnam Veterans of America favors passage. As you know, Mr. Chairman, VVA has always been in agreement with the Congress that

the commitment on the part of the Federal Government to assist veterans in the purchase of their first home is a vital readjustment program. It is VVA's belief that HR 2801 would serve that purpose well by lowering the threshold of entry into the housing market for low and moderate income veterans, for whom the Congress created this program forty years ago. It is the first time users of the VA program, to acquire their first home, that should be priority here. This proposal also has merit in that it should remove long standing "hard to move" properties from the VA's inventory, at the same time that it is aiding the effort to keep the revolving fund healthy by bringing in additional income.

If there is a "cost" to the government inherent in the measure known as HR 2801, VVA believes that it is primarily a "paper cost." The point is that foreclosed property that lacks a owner/occupant with a vested interest in maintaining the property deteriorates very quickly. Because the proposal takes account of market forces, in that only properties held for a relatively long time and reduced in price only then, the VA could realize actually more than under current practice, where some properties sit vacant for more than a year. Vietnam Veterans of America is particularly pleased that this measure is directed toward first time homeowners, which is the true target population of this readjustment program.

II. GAO REPORT NEEDED ON PREVENTABLE CAUSES OF DEFAULT

Mr. Chairman, the second major area that Vietnam Veterans of America wishes to address in the worrisome problem of a continuing high default and foreclsoure rate on loans guaranteed under the VA Home Loan Mortage Guaranty Program. As you will recall, Mr. Chairman, VVA has come before this body numerous times in the past few years advocating that the committee urge the VA to codify "Section F" of the VA Lenders Handbook, via the public rule making process. There is a building atmosphere now within the industry that would argue even more strongly for immediate action, in the mear future. Directly related to the need to codify these standards on "forebearance" is the lack of systematic information on who is actually going into default, and why. Are these folks who are losing their home familiar enough with the system to even know to ask for a "work-out" or any sort of forebearance? Have these folks sought and secured assistance from other areas in VA, or other elements of the veterans service network? The point is that nobody seems to have a good profile of why veterans are going into default and foreclosure. All of us are thrown back on anecdotal evidence and looking for answers as to how to solve the high default rate by looking to partial information.

Vietnam Veterans of America suggests to you, Mr. Chairman, that you call for a General Accounting Office Study of the "why" of veterans going into default and foreclsoure, focusing particularly on contributory problems such as PTSD, marital problems, employment, and other such difficulties where the VA has resources to materially assist in prevention of foreclosure, if only the veteran were properly matched with the service.

III. VVA SEEKS REDRESS FOR INDIVIDUAL VETERANS AND REFORM IN THE MANUFACTURED HOME INDUSTRY

As you know Mr. Chairman, Vietnam Veterans of America has sought redress through the courts for individual veterans who have been subject to fraud by members of the manufactured housing industry. In January and early February of this year, Vietnam Veteans of America first became aware that there were apparent widespread corrupt practices in the fabrication, billing, and financing of manufactured housing under the VA Manufactured Home Guaranty Program. VVA began to make inquiries and investigate both the nature and the scope of reported abuses. What we found were indications that the leading companies in the field were implicated, that the scope of the problem was nationwide, involving tens of thousands of veterans, and that the corrupt practices had been going on for as long as ten years.

The Veterans' Administration, Office of the Inspector General was actively investigating the charges. Working in association with the U.S. Department of Justice, criminal charges and claims for restitution were starting to be brought against the guilty parties. The problem was that the Government was only going after those cases where a default and foreclosure had occurred, and the VA guaranty invoked. The vast majority of veterans, who had been paying as much as $6,000 too much for their family's housing, would have no way to get their money back. In other words, they would have to continue to pay inflated payments to the people who had knowingly defrauded them. Otherwise, they and their families would be thrown out on the street. It is the strong conviction of Vietnam Veterans of America that this is an intolerable injustice, and must be redressed.

At the beginning of March of 1985, VVA decided to press ahead with the concept of a class action suit that would provide a remedy for those individual veterans who had approached us, and for the thousands more we had good cause to believe had also been defrauded. Special Counsel Daniel F. Hayes was retained by VVA, who along with his colleague Mr. Nicholas Gilman are lead attorneys on the case. Both Mr. Hayes and Mr. Gilman are Vietnam veterans. Mr. Gilman was severely wounded in Vietnam.

During March and April, other veterans who had been defrauded approached VVA, and the preparation of the initial complaint was completed.

On April 24, 1985, the complaint was filed in United States District Court, District of Delaware, as Civil Action #85-244, Chief Judge The Honorable Murray S. Schwartz presiding. Named as plaintiffs were Vietnam Veterans of America and five individual veterans who had been bilked and had approached VVA for assistance in seeking redress. As defendants were six (6) manufacturers, five (5) affiliated companies, and a member of the Board of one manufacturer. The Court was asked to certify classes on both sides of the suit.

Over the course of the summer many other veterans who had been bilked and defrauded by the unlawful practices of the defendants approached VVA for assistance. On August 26, 1985, an "Amended Class Action Complaint" was filed in the same U.S. District Court. A total of twenty-two (22) individual veterans were listed as plaintiffs.

VVA has asked for Injunctive Relief against the unlawful practice of "packing invoices" in this amended brief, to force the guilty parties to act in a lawful and proper manner henceforth.

Also named as defendants are three corporations that own "consumer conditional sales contracts." These three companies are the largest holders of these contracts for VA guaranteed manufactured homes, in a field where the largest twelve companies hold 86% of such contracts. These three corporations are named as class representatives. Under 16 CFR 433.1, a 1975 Federal Trade Commission Rule, the "holder in due course" can be held liable. Once final judgement is made, the holding companies can seek redress under their "recourse agreements" with the as many as 7,000 dealers are that involved.

This is where the suit rests today. Formal briefings are currently scheduled for October 3, 1985. It is worth further noting that "Racketeer Influenced and Corrupt Organizations (RICO) Act of 1970 claims have been served on all of the defendants. It is our belief that all of the defendants are liable under RICO and other theories of liability. The Supreme Court decision in "Sedima vs. Imrex," which was rendered in early July, cleared the way for us proceed under RICO.

The question does, arise, Mr. Chairman, of where does all this leave us? Vietnam Veterans of America filed the suit because of our outrage at these persons controlling this industry growing rich on the backs of those veterans who are, in terms of economic resources least able to fight back. Our first intent was to secure financial recompense for those veterans who had literally skimped on the baby's milk money in order to make the payments on their manufactured home. Our second intent was to help force the manufactured home industry to begin acting within the boundaries of what is just, proper, and lawful in their dealings with veterans. We shall, with the able leadership of Mr. Hayes, Mr. Gilman, and their associates at Smiley, Olson, Gilson, and Pangia, persevere until we have achieved these goals insofar as is possible in Federal Court.

However, the active oversight and strong leadership of this Committee is necessary in order to force a clean up in this area. Mr. Chairman, VVA is confident that you will display the same

tenacity and unwavering support for the average veteran in this matter as you have in saving the VA Home Loan Guaranty program from the Administration. VVA again thanks and commends you for your stalwart defense against the Administration's ill conceived attempt to unduly hike the "User Fee" tax on veterans. VVA trusts and believes that this body with your strong leadership, will be able to ensure that administrative changes are made that will force all concerned to at least act in a lawful manner, and with a modicum of decency.

VVA would suggest a number of recommendations for you to consider. First, that there be "on site" assessment of mobile homes, rather than merely looking at the invoices. Secondly, that there be stringent ongoing enforcement of all rules and regulations governing the behavior of dealers, manufacturers, and finance companies. Third, that those same rules and regulations be reviewed by VA, and, after full consultation with the Congress, amended as necessary in order to fulfill Congressional intent that this be an honest, well administered program. Fourth, that VA should, at minimum, act in such a way toward dealers and manufactuers that have been guilty of fraud that they are in essence on probation. Further, that VA should bar from the program any individual or entity that does not act consistently within the bounds of lawful and decent behavior.

One final note, Mr. Chairman, if I may Vietnam Veterans of America wishes to commend the Office of the Inspector General of the Veterans' Administration for their fine work in this matter. We note especially the excellent work of Assistant Inspector General Robert A. Hincken and the Office of Investigation in pursuing the investigation. Four corporations have pledded guilty to criminal charges. Articles in the financial press lead us to believe that the government is negotiating with as many as fifty other companies in regard to criminal charges, and has been so negotiating since the early Spring. We urge you, Mr. Chairman, to see to it that the VA and the Department of Justice move forward with these negotiations, so that the full scope of the problem becomes public. If this program is to be restored to integrity all responsible parties must get on with their part of the job. VVA urges you to seek assurance that the Executive Branch will proceed with alacrity.

Mr. Chairman, Vietnam Veterans of America thanks you for allowing us to present our views here today.

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STATEMENT OF
RICHARD F. SCHULTZ
ASSOCIATE NATIONAL LEGISLATIVE DIRECTOR
DISABLED AMERICAN VETERANS
BEFORE THE
SUBCOMMITTEE ON HOUSING
AND MEMORIAL AFFAIRS
OF THE
HOUSE COMMITTEE ON VETERANS AFFAIRS
SEPTEMBER 12, 1985

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

On behalf of the one million members of the Disabled American Veterans, may I say how very much we appreciate the opportunity to appear here today to comment on the VA Home Loan Guaranty Program, as well as legislation pending before the Subcommittee.

Initially, Mr. Chairman, the Disabled American Veterans wishes to commend you and the members of the Subcommittee for this timely exercise of your oversight responsibilities -- especially in light of recent disclosures of fraud and abuse in the VA Home Loan Guaranty Program -- and consideration of legislation to establish a discount sales program of homes held by the Veterans Administration.

H.R. 2801

Introduced by Mr. Sundquist on June 18, 1985, H.R. 2801 proposes, through appropriate amendment to Title 38, U.S. Code, to establish a discount sales program of homes held for an extended period of time by the Veterans Administration

As we understand it, H.R. 2801 will grant the Administrator the authority -- if in the best interest of the VA -- to establish a discount sales program of VA held properties whereby the Veterans Administration shall offer these properties to veterans who have not previously purchased a dwelling unit and who are eligible for the VA Home Loan Guaranty Program.

The discount price of properties to be offered for sale to eligible veterans is determined by the length of time the VA has offered these properties for sale to the general public. For example, properties offered for sale by the Administrator:

1. for at least three months but less than seven months shall be sold at a discount price that is not less than 80%;

2. for at least seven months but less than a year shall be sold at a discount price that is not less than 75%;

3. for at least a year shall be sold at a discount price of not less than 70%.

Mr. Chairman, while the DAV has no official position on H.R. 2801, we clearly recognize that the intent of this bill is to provide the Administrator with a tool to facilitate the expeditious sale of VA properties, thus helping to minimize a loss of revenue in the VA Loan Guaranty Revolving Fund, while, at the same time, providing an avenue for eligible credit worthy veterans to purchase a home at a discount.

The DAV certainly has no objection to the enactment of H.R. 2801. However, may we suggest including -- as a category eligible for the discount sales program proposed by H.R. 2801 --

government agencies and nonprofit organizations for the purpose of assisting veterans in need of essential services provided outside the formal VA medical facilities.

Mr. Chairman, veterans' service organizations, state and local government agencies, as well as other nonprofit groups, provide an array of services for our nation's veterans. The time has arrived to expand these traditional services to provide other forms of assistance needed by our aging veteran population.

As you are aware, the demand for health care and related services for aging veterans is rapidly increasing during a time when our government's fiscal ability to meet those needs is faltering.

Perhaps these foreclosed properties, now sitting empty, could be put to good use as adult day health care centers or community residential homes. Or, the VA's Department of Medicine and Surgery (DM&S) could utilize these properties as Outreach Centers, halfway houses or after-care treatment centers for veterans receiving treatment for chemical abuse and other related problems.

Mr. Chairman, we believe the inclusion of these groups as eligible to participate in a discount sales program of VA held properties could very well be the impetus needed to spawn new and innovative programs which would provide much needed non-institutional services for our nation's veterans, particularly

our aging veterans, while, at the same time, saving federal expenditures and reducing the VA's inventory of foreclosed properties.

However, in all frankness, Mr. Chairman, we are more concerned with the circumstances and causes leading to the large inventory of properties the VA now possesses due to foreclosure rather than alternative means to reduce the inventory. I will address those concerns later in my testimony.

VA HOME LOAN GUARANTY PROGRAM

As you know, Mr. Chairman, the authority for the VA's Loan Guaranty Program is set forth in Chapter 37 of Title 38, U.S. Code. The purpose of this program is to assist eligible veterans in obtaining favorable credit terms, without a down payment, from private lenders for the purchase, construction or improvement of homes to be occupied by veterans and their families.

There is no doubt that many veterans could not purchase a home without the VA's Home Loan Guaranty Program. Since its inception on June 22, 1944, this program has enabled over 11 million veterans to obtain a home loan.

By assisting millions of veterans in acquiring a home, the VA's Home Loan Guaranty Program has added stability and expanded the tax base of nearly every community in our country.

Veterans' use of the VA Home Loan Guaranty Program -- like private sector housing programs -- is subject to and directly

related to general economic conditions and, more specifically, to conditions in the financial and housing markets.

As we all know, within the past several years, the housing and financial markets have experienced shortages of mortgage funds, increased home prices and ownership costs, as well as realized the highest interest rates in history. Additionally, this same period was marked by unprecedented rates of high unemployment.

Veterans, like all Americans, have been adversely impacted by these economic conditions. As a result, there has been a dramatic decline in the number of home loans guaranteed by the VA (Fiscal Year 1982 was the lowest since 1944), accompanied by an equally heavy increase in home loan defaults and subsequent foreclosures.

Fortunately, those economic conditions have abated somewhat and mortgage funds are generally more available, interest rates are down from their record-breaking high in Fiscal Year 1982, and home prices have remained relatively stable. Additionally, the high rates of unemployment have also been reduced significantly.

Unfortunately, however, the VA Home Loan Guaranty Program continues to experience unusually large numbers of foreclosures that have adversely impacted on the Loan Guaranty Revolving Fund. And, due to the continued large number of foreclosures, the Congress last year found it necessary to approve supplemental

appropriations in order to replenish the depleted Loan Guaranty Revolving Fund.

Subsequently, the Congress further addressed the dilemma of the VA's Loan Guaranty Revolving Fund by enacting legislation -- Public Law 98-369, The Deficit Reduction Act of 1984 -- that increased the users fee from .5% to 1.0%, required the fee to be deposited in the Loan Guaranty Revolving Fund and extended authority to collect the fee through September 30, 1987. These provisions, together with others contained in Public Law 98-369 pertaining to acquisition of properties and vendee loans, all became effective over the past 13 months.

Quite frankly, Mr. Chairman, the DAV is most disturbed by recent disclosures of the VA's Office of the Inspector General concerning the Mobile Home Industry "kickback" scheme; the "equity skimming" scheme in southern California and the report on an audit of the VA appraisal system in Indianapolis, Indiana and Camden, New Jersey areas.

The VA's Office of the Inspector General has issued an interim report on its findings following an audit of the VA fee appraisal system (for the period October 1, 1981 to December 31, 1984) at Indianapolis, Indiana and the Camden, New Jersey areas.

This report reveals that of 8,700 residential loans guaranteed by the Indianapolis Regional Office during this period, 2,631

of the loans defaulted and 60% (1,576) were worth less at foreclosure than at loan origination, with 319 of those defaults decreasing at least 20% or more in value.

Furthermore, during the ongoing investigation in the Camden, New Jersey area by the VA, the Department of Housing and Urban Development's (HUD) Office of Inspector General and the Federal Bureau of Investigation (FBI) , they identified approximately 50 highly inflated and 10 false appraisal reports that were processed through the VA system and converted to HUD insured loans.

During this investigation, several realtors, real estate investors and developers were interviewed and questioned as to why VA fee appraisers were used when they knew that these properties were going to be sold using the FHA insured mortgages. In responding to this question, they indicated that the VA fee appraisers were "easier" and caused them less problems. One realtor stated that he favored the VA appraisal system because if the appraisal was converted to a HUD insured mortgage, there was little chance of the property receiving a VA staff review. The Inspector General's review of 500 VA fee basis appraisals in Camden confirmed that none had received a VA staff review.

This report further shows that of 43 properties reappraised by a VA appraiser and construction analyst, inflated appraisal amounts ranged from $2,200 to $10,400 per property and 10

properties were totally worthless (gutted) and were originally appraised by a VA fee appraiser to be worth between $24,000 and $33,000.

The Inspector General's report also points out that as a result of the decrease in value of these properties, the VA paid higher claim amounts than necessary, thus causing a greater indebtedness for the veterans who lost their homes through foreclosure.

Mr. Chairman, we are also greatly disturbed by an article published August 12, 1985, by Forbes magazine in which they report, "A VA insider estimates one-third of the 25,000 VA foreclosures last year involved some sort of fraud, ranging from falsification of homebuyers' creditworthyness to overvaluation of properties." This same article revealed, "In the words of one veteran thrift chairman, 'The real estate business has always been a dirty business.'" The article further stated, "The danger has always existed of a real estate broker's eyeing a $12,000 commission on a $200,000 home sale and helping the prospective buyer's credit look better than it was, or helping to phony the real downpayment, or (aided by a dishonest property appraiser) overvaluing a home."

It is evident, Mr. Chairman, that veterans -- who are making the largest financial investment most of them will ever make -- are prey to those unscrupulous, scheming individuals and companies who seek to profit illegally at their expense.

Mr. Chairman, we are also concerned with the VA's process of guaranteeing loans. As we understand it, the VA has no standard guidelines to insure that only credit worthy veterans receive loans. Also, there is no system that identifies loan applications, submitted to the VA through the prior approval basis, that have been previously denied by lenders utilizing the automatic approval program.

This, Mr. Chairman, causes a situation whereby veterans who have had their loans rejected by VA lenders using the "automatic program" have resubmitted their loan applications to another VA authorized lender who, in turn, approves the veteran's loan or submits it to the VA on a prior approval basis.

We believe the absence of a system set by the VA to identify previously rejected loans, combined with the absence of a reasonable credit standard, adds to the high rate of defaults by veterans.

Yes, Mr. Chairman, it is clear that there are individuals and companies who wish to illegally profit at the expense of veterans and the Veterans Administration. Therefore, we feel that further steps need to be taken to insure the solvency and integrity of the VA Home Loan Guaranty Program, as well as assure that credit worthy veterans who wish to purchase a home utilizing this program can do so.

Keeping this in mind, we must examine what steps are being taken to minimize the risk of financial loss to the veteran and the Veterans Administration. Specifically, we must ask a number of questions that have a direct bearing on this issue:

1. Does the VA have a standard loan originating policy?

2. What effort is the VA undertaking to insure that veteran home buyers eligible for the VA Loan Guaranty meet reasonable credit standards prior to purchase of a home?

3. Are mortgage bankers using the same stringent standards for the VA Home Loan Guaranty as they are for commercial loans?

4. Has the VA evaluated foreclosed loans to determine the causes of veterans defaulting on their loans?

5. Has the VA -- in light of the great number of VA foreclosed properties decreasing in value -- taken steps to develop uniform guidelines to monitor, evaluate and document fee appraisals?

6. We understand that it can take the VA and the Justice Department six months to five years to finalize foreclosure actions. What actions are both agencies taking to improve their timeliness of completing these foreclosures?

7. Following foreclosure action, how actively does the VA pursue collecting the debt that has resulted from the foreclosure?

8. What is the overall effect of the provisions of the Deficit Reduction Act of 1984 (P.L. 98-369) on the Loan Guarantee Revolving fund?

Mr. Chairman, we believe the answers to these questions could very well lead to administrative or, perhaps, legislative improvements that could result in substantial savings for veterans and the Loan Guaranty Revolving Fund. This is especially true if: collected debts were deposited in the Loan Guaranty Fund;

foreclosure actions were completed in a timely manner; only credit worthy veterans were approved for loans and veterans in default were to receive greater assistance in counseling from the VA. Of course, all these improvements would have to be accompanied by the development of strict, uniform guidelines for VA fee appraisers.

Further Recommendations

As stated earlier, Mr. Chairman, the VA's Inspector General has been investigating the Mobile Home Industry "kickback" scheme, the "equity skimming" scheme in southern California and the VA fee appraisal system.

These schemes and questionable fee appraisal practices are defrauding veterans and the Veterans Administration. We believe it only appropriate to utilize the funds collected from those who have violated the law to help the Loan Guaranty Revolving Fund which has been directly impaired as result of these schemes.

In this regard, Mr. Chairman, we would strongly urge you and the Subcommittee to take appropriate action to provide legal authority for the VA to deposit such funds in the Loan Guaranty Revolving Fund.

Furthermore, we believe that a legislative remedy is necessary to identify and assist those veterans who have already lost their homes through foreclosure and were victims of these fraudulent schemes.

In summation, Mr. Chairman, we would like to again say that the VA Home Loan Guaranty Program has provided valuable and much needed assistance to our nation's deserving veteran population. We also realize that the VA Home Loan Guaranty Program is experiencing financial difficulties due to the large number of foreclosures which we believe is caused, in part, by the lack of a standard loan originating policy, questionable fee appraisal activities and by those who wish to make a profit at the expense of veterans and the Veterans Administration.

We therefore urge you, Mr. Chairman, and the members of this Subcommittee to take the necessary action to assure that this nation's deserving veterans continue to have the benefit of a well-managed and financially sound VA Home Loan Guaranty Program.

This concludes my statement, Mr. Chairman. I again wish to thank you and the members of this Subcommittee for allowing us this opportunity to express the DAV's views on this important subject.

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PARALYZED VETERANS
OF AMERICA
Chartered by the Congress
of the United States

STATEMENT OF

R. DENNIS SMURR, ASSOCIATE LEGISLATIVE DIRECTOR

PARALYZED VETERANS OF AMERICA

BEFORE THE

SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS

OF THE

HOUSE COMMITTEE ON VETERANS' AFFAIRS

CONCERNING

OVERSIGHT OF THE VA HOME LOAN GUARANTY PROGRAM

SEPTEMBER 12, 1985

Mr. Chairman and Members of the Subcommittee, on behalf of the members of Paralyzed Veterans of America, I want to thank you for this opportunity to present the views and concerns of PVA regarding the current activities of the Veterans Administration Home Loan Guaranty Program. I am Dennis Smurr, PVA Associate Legislative Director.

At the outset, Mr. Chairman, PVA would like to commend you for holding this hearing and for your dedicated, insightful leadership. In addition, we wish to further compliment you and each Member of this Subcommittee for your ongoing efforts to improve the scope and effectiveness of this important benefit that affects so many of our nation's veterans.

The VA "Home Loan Guaranty" is a veteran entitlement program, available to all veterans, who meet the statute requirements. Since its inception in June of 1944, the VA Home Loan Guaranty Program has assisted more than 11 million veterans obtain suitable and affordable, private housing.

It has been one of the most successful housing programs in this nation's history, and the vast majority of loans guaranteed have cost taxpayers only the minor administrative cost of processing the initial loan. During its 41 year history, only four percent of all the loans guaranteed under this program have resulted in foreclosure. Without a doubt, the VA Home Loan Guaranty Program has been a good investment in America, providing stability and expanding the tax base of nearly every community in our country.

The purpose of today's hearing is to examine the VA's current property management practices and to determine what, if any, changes need to be made to the program's future financing arrangement. In addition, the legislative proposal, H.R. 2801, a bill introduced by the Honorable Don Sundquist, to establish a discounted VA sales program on foreclosed properties for veterans, will be considered. And importantly, attention will be focused upon the recent frauds, which have been perpetuated against veterans and the VA by the manufactured housing industry.

Mr. Chairman, it is safe to say that the VA Home Loan Guaranty Program has, in the past 18 months, endured some of the most trying times of its 41 year existence. For example, in March 1984, as a result of the recent recession and an unprecedented number of property foreclosures, the VA had a record-

high inventory portfolio of 22,316 properties valued at over $800 million. Since the beginning of the fiscal year, the VA Loan Guaranty Service has, as of August, sold more than 24,000 properties, which has generated revenues of $1 billion. This, in part, can be attributed to the nation's overall economic recovery, but PVA believes that credit must also go to Robert M. O'Toole, Director, and to the employees of the VA Loan Guaranty Service.

Mr. O'Toole and his staff have instituted some innovative management practices that have resulted in a positive attitude within the VA Loan Service, all of which has helped bring about a dramatic turn of events in the VA inventory portfolio. Through the use of paid sales commissions, cash discounts, concentrated management task force operations, and auctions of hard-to-sell properties from the portfolio, the Loan Guaranty Service has reduced its current inventory to approximately 18,000 units. This is most noteworthy in light of the fact that new foreclosures continue at a very high rate.

We feel confident that the VA Home Loan Guaranty Program, with its renewed vitality, can do well in meeting the rigorous demands that continue to menace the future of the American housing market. This leads us to the consideration of H.R. 2801, proposing a broad-base discount sales program.

In reviewing H.R. 2801, PVA can see merit to the bill, but we do not think that such legislation needs to be enacted at this time. The VA already has the administrative discretion to discount the sale price of properties in its inventory portfolio, and it can exercise this authority on a case-by-case basis. We feel this approach is more prudent and economically advantageous

than that which is proposed in H.R. 2801. In addition, we view H.R. 2801's stipulation, limiting such a discounted sale to "a veteran who has not previously purchased a dwelling unit," as being discriminatory. To be fair to all veterans, provision must be made in H.R. 2801 to address the veteran who may have lost a guaranteed home due to divorce, unemployment or disability. These veterans are just as deserving of the benefits of such a discounted sales program as those currently addressed under H.R. 2801.

The VA Loan Guaranty Service, under its existing authority, might want to borrow language from H.R. 2801 and establish a similar discount program. To incorporate such a program, on a regional basis, as individual inventories dictate, certainly has positive merit. Such a program could be activated by a triggering mechanism at VA Central Office on the basis of a predetermined inventory threshold - one that would reflect current real estate marketing trends and the economic conditions existing within each region of the United States. The affected VA Regional Office could then make available to interested veterans, through private notice or public advertisement, a listing of those properties that are to be released, stating the timeframe and the discounted sale price that prevails on each.

The VA may have to resort to additional innovative property management practices if it is true that home foreclosures could become even more widespread. For example, the August 26, 1985, issue of U.S. News & World Report, estimated that, nationwide, 300,000 foreclosures would be initiated this year alone. Therefore, provisions similar to those contained in H.R. 2801 may need to be instituted sometime in the future; but, until such

conditions dictate, PVA would rather have the VA Loan Guaranty Service retain its discretionary authority in handling its foreclosed property portfolio.

As to the issue of the fraud which as been perpetuated against veterans and the VA by the manufactured home industry, PVA states, unequivocally, that we support and applaud the efforts of the VA Inspector General and his staff for their efforts to bring to justice those manufacturers who have violated the law. We especially want to compliment the VA Home Loan staff in the Atlanta, Georgia VA Regional Office for uncovering this practice and referring it to the VA Inspector General.

It is also noteworthy to mention the current class-action suit against several mobile-home manufacturers for recovery of fraudulent overcharges collected from veterans on previously purchased mobile-homes. This court action is very admirable in light of the fact the VA can only pursue similar court action against manufacturers in cases where the veteran had defaulted on his loan and the VA, subsequently, had taken title to the mobile-home.

Since 1981, the VA has taken title to some 3,000 manufactured homes which veterans have lost through foreclosure. It would be very difficult indeed to correlate how many of these foreclosures came about as a result of the over-pricing practices with which the industry is being charged. Still, the fact remains, the manufactured housing industry has admitted to invoice padding and dealer kickbacks, therefore, veterans have been affected and the solvency and creditability of the entire Home Loan Guaranty Program suffers.

According to testimony presented before this Committee last March by the National Manufactured Housing Finance Association, more than 92,338 loans have been financed under Section 1819 of Title 38, the manufactured home loan guaranty program, since its creation by the enactment of Public Law 91-506, the "Veterans' Housing Act of 1970." This figure does not include those manufactured homes that were permanently affixed to a lot, and handled as a real estate transaction under Section 1810 of Title 38, the regular VA single-family loan program.

We are, therefore, presented with a sizable problem and one with serious implications. Especially now that half the nation's major mobile-home manufacturers have offered to plead guilty to criminal charges of padding sales invoices and defrauding the Veterans Administration. This is indicative of two facts: the fraudulent practice is widespread; and, maybe the invoicing policy of the VA for the purchase of manufactured homes needs to be reviewed and possibly revised.

If this be the case, then PVA would hope that an industry-wide organization, such as the Manufactured Housing Institute or the National Manufactured Housing Finance Association, would be willing to work with the appropriate Veterans Administration officials to develop a better invoicing method, if that is what is needed. But more importantly, the manufactured housing industry needs to initiate an aggressive campaign to police its own member manufacturers to rid itself of present questionable practices to avoid future improprieties and to reestablish itself, not only with veterans, the Veterans Administration, but with the American public, in general.

Mr. Chairman, that concludes PVA's testimony. We appreciate the opportunity to testify, and hope that our concerns and recommendations will be considered when you make constructive changes to this Veterans Administration program so as to improve the benefit to all veterans.

Thank you, Mr. Chairman, and I will be glad to answer any questions I can.

VETERANS OF FOREIGN WARS OF THE UNITED STATES

STATEMENT OF

DENNIS M. CULLINAN, SPECIAL ASSISTANT
NATIONAL LEGISLATIVE SERVICE
VETERANS OF FOREIGN WARS OF THE UNITED STATES

BEFORE THE

SUBCOMMITTEE ON HOUSING AND
MEMORIAL AFFAIRS
COMMITTEE ON VETERANS' AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

WITH RESPECT TO

THE IMPACT ON VETERANS OF FRAUD
IN THE MANUFACTURED HOUSING
INDUSTRY AND H.R. 2801

WASHINGTON, D. C. SEPTEMBER 12, 1985

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

On behalf of the membership of the Veterans of Foreign Wars of the United States, I wish to express our appreciation for having been afforded the opportunity to appear before this most distinguished and industrious Subcommittee so that we may work together in the service of this Nation's veterans. Today I will present our views on the abhorrent fraud perpetuated on veterans by certain unscrupulous profiteers in and associated with the manufactured housing industry. Additionally, H.R. 2801, introduced by the Honorable Don Sundquist of this Subcommittee, which would benefit veterans by establishing a discounted sales program of certain homes by the Veterans Administration for veterans, will also be addressed.

It is our view--and it would seem to us an indisputable point of fact--that the VA Home Loan Guaranty Program is one of the most successful and beneficial VA programs serving veterans. There can be no doubt that if it weren't for this

program a good many veterans would not be in their own homes today. And one of its key elements is the availability of guaranteed loans for the purchase of manufactured homes.

It has always been true, but particularly today in light of the rapidly escalating cost of housing, a manufactured home is often all a veteran can afford. When competent and reputable individuals are responsible for their production and sale, they may be affordable, nicely furnished dwelling. Unfortunately, swindlers in this industry have been defrauding unsuspecting veterans--predominantly lower income veterans--for years and in many instances turned the American dream of home ownership into a nightmare of debt and foreclosed home loans.

One method used in bilking veterans out of their meager resources is known as "packing." That is, manufactured-home makers inflate their invoices, receive payment and later return some of the money to the dealers for taking their products. This kickback practice, it is reported, added between $200 and $5,000 to the price of a maufactured home, and usually averaged $1,000 to $2,000.

These "packed" invoices enable dealers to illegally exceed their profit limit by overcharging veteran buyers. Veterans pay more than these homes are worth with loans that are often much more than they can handle. The added burden of inflated mortgage costs forces many veterans to default on their loans and loose their homes. A compounding evil is that VA Home Loan Guaranty Revolving Fund (HLGRF) is further depleted by having to absorb the enourmous costs of thousand upon thousands of bad loans. Individual veterans along with one of their most beneficial programs both come to bear the brunt of this criminal activity.

Another form of invoice padding is charging for non-existent items. The price of a manufactured home is inflated by adding the cost of illusory accessories--such as washing machines, dryers, air conditioners and other items--to the invoices

that are submitted to the VA. The unfortunate result of this particular scam is just the same as the first--both the veteran and the VA are cheated out of much needed dollars.

Investigators contend that these schemes have gouged more than $100 million from buyers, the federal government and conventional lenders. VA officials suspect that manufacturers padded the invoices for 80% or more of the 295,000 homes shipped last year.

The Veterans of Foreign Wars is absolutely appalled by these activities and adamant that those responsible be prosecuted to the full extent of the law and that proper compensation and restitution be made to all veterans who have been so victimized and to the VA HLGRF itself.

We are also of the opinion that steps to prevent such abuse are long overdue and should be initiated immediately. It may be late, but it is certainly not too late to ensure that veterans purchasing manfactured homes are never again taken advantage of this way.

Currently the VA allows dealers a 20% profit above the invoice price--but it is the manufacturer who determines this amount. This is like setting a bowl of candy before a child with a sweet-tooth, telling him not to eat any and then walking cheerfully away while mentioning you won't be back to check on him. Nonsense--it is precisely this sort of nonchalant approach which allowed this packing fraud to go undetected for so many years.

We believe the first step toward eliminating this particular scam is by financing manufactured homes the same as are site-built homes--based on individual appraisals rather than on manufacturer's invoices. Further, we would like to see closer monitoring of the manufactured-home industry with an eye toward at least providing veterans with a listing of reputable manufacturers and dealers. It

would also be well advised to provide veterans who are about to purchase either a manufactured or site-built home with a VA counselor or adviser to fully apprise him of all the obligations, responsibilities and potential pit-falls of buying and owning a home. The pamphlets and other written materials currently available, although admirable, are not sufficient by themselves given the complexity of such a transaction along with the attendant excitement of making, what is for most people, the largest purchase of a lifetime.

The VA Home Loan Guaranty Program has proven to be of inestimable value to home buying veterans and to the American economy. The fraud perpetuated by elements of the manufactured-home industry constitutes a viscous attack on the well-being of many thousands of veterans and on the continuing existence of one of their and the Nation's most worthwhile enterprises. The VFW is, therefore, adamant that full compensation and restitution be made to all concerned veterans and also to the VA Home Loan Program. Further, all possible measures must be taken to ensure that this and other forms of fraud and abuse are never allowed to happen again.

Also of discussion at this time is legislation introduced by a distinguished member of this Subcommittee, the Honorable Don Sundquist. This bill, H.R. 2801, would establish a discounted home sales program by the VA for veterans who are buying their first homes. Inasmuch as this would both benefit veterans and the VA Home Loan Program by reducing its holding time of certain real properties and consequently costs, it enjoys strong VFW support. We highly commend Mr. Sundquist for having devised and introduced this innovative and constructive measure.

Mr. Chairman, once again, thank you for holding this hearing and for requesting the participation of the Veterans of Foreign Wars. This concludes my testimony, and, I will be happy to respond to any questions you may have.

Statement of

The American Legion

1608 K STREET, N. W.
WASHINGTON, D. C. 20006

by

E. PHILIP RIGGIN, DIRECTOR
NATIONAL LEGISLATIVE COMMISSION
THE AMERICAN LEGION

before the

HOUSE VETERANS AFFAIRS COMMITTEE
SUBCOMMITTEE ON HOUSING AND MEMORIAL AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

on

MANUFACTURED HOUSING FRAUD AND VA
PROPERTY MANAGEMENT

September 12, 1985

Mr. Chairman and Members of the Subcommittee:

As always, The American Legion is pleased to have the opportunity to present its views on the VA home loan program for your consideration. The topics of today's hearing are timely in that the recent revelations of fraud by the manufactured housing industry should be carefully examined, and where fraud has been committed the guilty should be stiffly penalized.

Also, the general subject of VA property management practice is very important, noting the size of the VA's inventory of foreclosed properties. Anything that can be done to expedite the sale of these properties will surely bolster the Loan Guaranty Revolving Fund (LGRF) and the Direct Loan Revolving Fund (DLRF). In that regard, legislation, H.R. 2801, designed to expedite sales of foreclosed property by establishing a schedule of discounts on properties which are difficult to sell is an important contribution to the growing dialogue on how VA should dispose of its inventory.

Dating back to last February the VA's Office of Inspector General has undertaken an active investigation of possible widespread fraud in the manufactured housing industry. Since that time several indictments have been handed down and several manufactured housing makers have pled guilty or plea bargained their way out from under serious criminal charges of racketeering.

It is unclear to us where the VA currently is in its investigation or how VA now plans to proceed, but we applaud the VA for moving forward. As a result of the VA investigation, the practice of manufacturer kickbacks to dealers of mobile homes is believed to be a widespread practice throughout the industry. In The American Legion's view, this activity must be brought to a halt even if it means permanently suspending mobile home makers from the VA home loan program and even if it means jail for the perpetrators.

While it is impossible to say with certainty how long both VA and veterans buying mobile homes have been bilked by manufactured housing makers and dealers who overcharge veterans for the properties sold, it is clear that the practice

is a shameful example of corruption. As we understand it, mobile home builders are allowed by VA regulations a 20 percent profit markup. The American Legion has no quarrel with a legitimate business enterprise seeking to turn its best possible profit depending on what the market will bear. However, these home builders have systematically misrepresented the value of property by inflating the property invoices. As such, properties are sold using invoices provided to VA showing many extras such as washing machines, dryers, air conditioning, metal exterior skirting, outside decks and several other extras which are never finally provided.

This inflated invoice then justifies a loan guaranty greater than what is proper. For VA, this has meant the overexpenditure of guaranty dollars in cases of foreclosure. For the veteran, it means purchasing a property for more than it's worth, sometimes causing excessive mortgage costs that bring about default and even foreclosure. It appears as though after VA has guaranteed the loan and the veteran has made the purchase of the overpriced mobile home (overcharges that have been reported to range between $500 and $5,000 per property), the dealer receives a kickback from the funds generated by the overpricing scheme. As far as we know, the VA's Inspector General investigation has thusfar addressed the mobile home builders because of the misrepresentation of property value on invoices. If it hasn't already done so, that investigation should also encompass the price fixing among manufacturers and dealers who both benefit from the scheme.

Although we applaud the steps taken by VA to correct the problem, we are disappointed that VA was not able to uncover these fradulent activities sooner. Under current procedures, mobile homes are assessed for their value by appraisers under contract with the VA prior to providing a guaranty. The appraisers apparently have failed to look beyond the misrepresented invoices when they determine the value of a mobile home. If VA provided the kind of rigorous inspection on mobile homes that it provides for new single family dwellings in

attempting to assure the value of new home conveyances, this problem could have been uncovered much sooner and at much less cost to the VA and the cheated veterans having purchased overpriced mobile homes.

In that regard, we think the VA should undertake an evaluation of the quality of appraisals and qualifications of the appraisers with whom it contracts for property value assessments. One important step in this direction would be to undertake inspections of mobile home properties, both new and used. This recommendation is entirely consistent with earlier Legion suggestions that VA inspect new and used traditional dwellings.

The last time this committee held oversight hearings on the VA home loan program, VA testified in part on the progress it was making in the sale of its inventory of foreclosed properties. At the time, the agency stated that it was devoting greater resources to the marketing of these properties and was offering special sales of these properties in different locations around the country. These activities were said, at the time, to be helping the VA in disposing of these properties. The American Legion was encouraged by these developments and sincerely hopes that VA has been successful.

Legislation introduced on June 18, H.R. 2801, is intended to augment the tools already available to VA in the marketing of foreclosed properties. This measure would provide a property price discount scale to aid in marketing difficult-to-sell properties. As such, any home not sold within 3 to 6 months would be discounted by 20 percent; within 7 to 12 months, discounted by 25 percent and if unsold for over a year, discounted by 30 percent. This legislation would apply the discounted prices on these properties for first time homebuying veterans only.

The American Legion basically views this bill as a good faith step in the right direction, one which properly recognizes the economic constraints of the first time homebuying veteran. Its secondary focus appears to be directed toward inventoried properties which are hard to sell. Both of these

are legitimate considerations, but certain protections must be guaranteed when this legislation moves forward.

First, it should be made clear that nothing in H.R. 2801 is intended to restrict current VA procedures designed to quickly sell inventoried properties. Second, the quality of properties sold under provisions of this measure must be assured. Presumably, if a foreclosed property has been aggressively marketed by VA and has remained in the inventory for an extended period, the property is likely to be defective in its structural integrity or from a habitability standpoint. Since the veteran pruchaser under provisions of H.R. 2801 would use the property as a principal residence, VA must guarantee that the property is in "livable" condition.

While the discounts in the pending measure are substantial, there may be economically-depressed localities around the nation in which greater discounts would be necessary to stimulate first time veteran / buyer interest. We, therefore, recommend that this subcommittee consider granting authority for greater discount rate flexibility, especially on properties inventoried for more than seven months. Hopefully, greater discount flexibility would encourage sales before properties are rendered virtually unmarketable because of physical deterioration.

Mr. Chairman, that concludes our statement.

THE NON COMMISSIONED OFFICERS ASSOCIATION OF THE UNITED STATES OF AMERICA

"STRENGTH IN UNITY"

Statement of

Richard W. Johnson, Jr.
Director of Legislative Affairs

before the

Subcommittee on Housing and Memorial Affairs
Committee on Veterans Affairs

on

Loan Guaranty Oversight
September 12, 1985

NATIONAL CAPITAL OFFICE
219 N. Washington Street • Alexandria, VA 22314 • Tele: (703) 549-0311

Mr. Chairman: The Non Commissioned Officers Association of the USA extends to the committee and its staff our appreciation for the very active role this committee has assumed in supervising the veterans home loan guaranty program. Certainly, without this committee's unique understanding of the problems encountered in administering the program over the past few years, veterans would have suffered its loss. By its steadfast support, the committee has managed to preserve the program for the benefit of all veterans with only minor changes and improvements. NCOA is grateful for your efforts.

Today's hearing is another demonstration of the committee's continuing oversight of what is viewed by some to be a very troubled program. In this context, NCOA will discuss three primary areas of concern to the Association. First, the Association is concerned with the future of the loan guaranty program itself and the options which may be exercised to preserve its value to veterans. Second, NCOA is concerned with the VA's handling of the fraudulent price certification investigation of manufactured home builders. Finally, the Association will discuss the adequacy of the current $27,500 maximum guaranty.

FINANCING

Mr. Chairman, a recovery, albeit small, is underway in the loan guaranty revolving fund (LGRF). In recent months, the inventory of homes held by the VA has declined from about 22,000 to about 18,000. The foreclosure rate has also decreased considerably. Yet, the problems faced as a result of the recession may recur at any time. As a result, the LGRF will continue to require periodic appropriations to remain solvent. However, Congressional action can make the fund solvent and, perhaps, self-supporting again.

Underwriting Practices and Fees

Modified underwriting practices and increased fees hold no long term solutions to solving the problem. Creating new criteria or making existing criteria more restrictive will simply reduce the number of veterans qualified for loans. Historically, veterans loans have been a much better financial risk than other federally insured loans. At the same time, underwriting errors account for a relatively small percentage of loan defaults. More often marital problems or financial problems precipitated by an unpredictable event prompt foreclosure actions.

In the conventional mortgage industry secondary market mortgage traders and private mortgage insurers are beginning to increase qualification standards required for home mortgages. As noted recently, one of the largest private mortgage inusrers discontinued new policy issues because of major losses. But this effort is directly related to unusually high losses caused by creative financing arrangements which do not exist in the VA program. Each of the changes made in the conventional mortgage industry is targeted at reducing the number and circumstances under which adjustable rate mortgages (ARMs), Graduated Payment Mortgages (GPMs) and seller buy-downs (of interest rates) are used. These efforts are the conventional mortgage industry's attempt to reduce foreclosure rates which have grown at more than five times the rate of increase in VA foreclosures and have cost more than $500 million in private mortgage insurance losses.

The fee issue is one which has been widely discussed this year and, hopefully, rejected with some finality. Increased fees would be an unfair tax on veterans which would not raise enough revenue to salvage the program. Indeed, such fees would probably debase the program, enticing only the poorest credit risks to participate, thus exacerbating its purpose.

The Economy

The real, long-term, solution to restoring solvency in the LGRF is to eliminate the causes and effects of recession and mortgage foreclosures--high unemployment, high interest rates and inflation.

Since WWII the nation has suffered several recessions and recoveries. During each recession and for a period thereafter, home mortgage foreclosures rose to unusually high, but predictable levels. After each recession, as interest and unemployment rates declined, and as inflation and salaries continued to grow, mortgage foreclosures declined. However, the U.S. has had a very different kind of recovery from the 1982 recession. Unemployment has remained over seven percent and while many will be quick to report substantial increases in the number of new jobs, the quality of employment has declined. In the past few years more than one quarter million manufacturing jobs have been exported only to be replaced by service positions which offer significantly less pay. Inflation which results in increased home values and, usually, higher salaries has been reduced. Thus, the value of home ownership, particularly for mortgages with a high loan-to-value ratio, have declined considerably. Finally, interest rates have remained high, perhaps artificially high. Virtually all of this is the result of a propensity to deal with problems in the short-term. **The U.S. cannot continue to spend 21 percent of its Gross National Product while taxing only 17 percent. In short, the same economic policy that is responsible for the failure of 38 percent of this nation's savings and loan institutions and 25 percent of its banks is responsible for the current problems in the loan guaranty revolving fund.**

Accordingly, the real solution to the problem is to either raise federal taxes or reduce government spending. Regretably these efforts seem lost to both economists and legislators. **In other words, the rate and number of foreclosures will always be driven by economies which cannot be controlled by the VA. The solution to reducing forclosures is directly related to a long term improvement in the economy.** However, Congress can mitigate the need, frequency and amount of the appropriations required. The LGRF may even become profitable again if a long term change is made in both policy and management.

VA Loan Portfolio

NCOA recommends that the Veterans Administration be allowed to maintain its portfolio and, concurrently, be given the authority to manage the portfolio in accordance with good business decisions instead of Office of Management and Budget (OMB) guidelines.

In several previous appearances before this committee the NCOA has repeatedly stated its support for the VA loan guaranty program. In each previous appearance, the Association has noted the three main goals of the program. The first is to help veterans find suitable housing; the second is to assist veterans in keeping the house they have purchased; and the third is to manage the program in such a manner as to minimize its cost and assure its effectiveness. Obviously, the program is working.

Nearly 12 million homes have been financed with VA guarantees. The total investment of more than $200 billion has benefited the tax base of almost every city and town in the nation. Additionally, the VA has an aggressive counseling and assistance program for veterans who need help in retaining their home. Finally, within the limits placed on management of the

program, the VA has done a magnificent job in controlling its costs. Indeed, it has cost less than $100 for every veteran participant in the program.

However, several years ago, the VA was directed to close its loan portfolio. The decision was made to create an influx of revenue into the government and avert the need for appropriations into the fund during the recession. Yet in examining that decision with 20/20 hindsight, it is easy to see that the profits derived from management of the portfolio provided the operating expenses for the program for many years. As a result, a program that was never designed to be self supporting, went so long without an appropriation that almost everyone has forgotten its foundation!

Program management of the VA's loan portfolio may not immediately provide funds sufficient to avoid appropriations. It will, in fact, require an appropriation. Still, over the course of time, it will allow the VA to profit from the loan guaranty program and minimize the number and amount of future appropriations. Integral to a decision to manage the portfolio must be a decision to insulate its operation from external interference.

During the period when last the VA operated its own portfolio, many sale and liquidation decisions were driven by an OMB "fire-sale" mentality. Instead of using good business judgment to manage the sale of loans, decisions were driven by budgetary requirements. OMB, by our understanding, frequently ordered loan sales during soft market periods to achieve better short-term budget statements. This is not only poor management, it is also expensive. If external interference is precluded by law, the VA could manage a portfolio which once again will support the loan guaranty program.

MANUFACTURED HOUSING INVESTIGATION

In recent months the Veterans Administration, particularly the office of the Inspector General, has done an outstanding job of identifying a systematic fraud in the manufactured housing industry. The fraud generally involved a false certification given by the manufacturer to the retailer. The falsely inflated price, then used as the basis for computing sale price, created overcharges ranging from several hundred to several thousand dollars. Having identified this problem the VA has been able to secure from some of the offending manufacturers financial settlements and fines in sufficient amount to offset the losses the VA has suffered from paying guarantees on defaulted loans. In turn, the VA has used these recoveries to reduce the indebtedness of many veterans who defaulted on manufactured housing loans. For its efforts, NCOA commends the VA. However, the Association believes the VA has stopped short of its objective.

The efforts made by the VA have resulted in restitution only for the actual loss suffered by the VA as a result of guaranty payments made after a loan has been foreclosed. While the VA has assured the Association of its desire to gain criminal prosecution for false certifications of prices on loans which have not fallen into default, the VA has advised NCOA: "U. S. Attorneys have told us repeatedly that violations of this magnitude do not alone warrant federal prosecution." The VA also noted such prosecution would not result in restitution to individual veterans who have suffered losses as a result of the false certifications, but would result only in fines from which the U.S. would benefit. Nevertheless, NCOA believes the VA and the government has a proprietary interest in this issue.

According to the VA: "There is substantial evidence that false certifications have been made in connection with the sale to veterans of many new mobile homes." These false certifications have been made to the government in a federally sponsored program and morally require prosecution. Selective enforcement of laws should not be a privilege of government, particularly when only a partial settlement has been reached on behalf of the victim. Surely, veterans who are still paying on their homes, at higher levels than can be legally justified because of a fraud committed against the government, are victims entitled to equal protection. The VA and the government have a fiduciary interest in seeking full restitution on behalf of veterans who were defrauded, not just the unfortunate few who have defaulted on loans guaranteed by the government.

It would be fairly simple for the committee to direct the VA to seek voluntary refunds from the companies in question to all veterans who were victims of this fraud. It would also be fairly simple for the committee to direct federal prosecution of those individuals and companies who do not wish to make voluntary refunds. NCOA recommends this course of action.

Finally, with regard to this matter, it is important to both the manufactured housing industry and veterans to have this issue resolved as quickly as possible. In the absence of concise action, the manufactured housing industry will suffer and veterans will become increasingly less welcome as consumers in this market. Therefore, NCOA suggests that every effort be made to determine a quick and decisive solution.

LOAN GUARANTY AMOUNT

The Association will not dwell on its last area of concern since the committee has previously acted to increase the $27.500

ceiling on loan guarantees. However, NCOA reminds the committee that new housing costs have increased more than 125 percent since 1974, according to the National Association of Home Builders. During the same period, the VA guaranty maximum has increased only 57 percent. At the same time, average loan amounts have risen nearly 150 percent. As a result, veterans have been "priced out" of many housing markets.

NCOA appreciates the effort made by this committee last year to provide a modest increase in loan guaranty coverage. We urge the committee to renew its efforts in hopes the Senate will concur. This legislation must be passed if the veteran is to remain competitive in home purchases.

CONCLUSION

Thank you for allowing NCOA this opportunity to comment on the VA home loan guaranty program. The Association strongly believes the program is sound in its current structure but would benefit greatly if the VA is allowed to maintain its own portfolio. NCOA encourages the committee to accept its recommendations on this issue. Equally important, NCOA believes everything humanly possible should be done to resolve the investigation of manufactured home builders in a manner satisfactory to all veterans--not just those who have defaulted on their loans. Finally, NCOA urges the committee to renew its efforts to gain an increase in the maximum guaranty amount.

Office of General Counsel Washington D.C. 20420

Veterans Administration

In Reply Refer To

OCT 21 1985

Honorable Richard C. Shelby
Chairman, Subcommittee on
Housing and Memorial Affairs
Committee on Veterans' Affairs
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Enclosed please find the Agency's response to a portion of the questions you submitted following the September 12, 1985, hearing on the VA home loan guaranty program. Answers to your questions #5 and 11, and to Representative Smith's questions #3, 5, and 6 will be forwarded to you as soon as possible.

I appreciate the opportunity to provide additional information for the record.

Sincerely yours,

DONALD L. IVERS
General Counsel

Enclosure

WRITTEN COMMITTEE QUESTIONS AND THEIR RESPONSE

Questions from Chairman Shelby

Question 1. The VA's circular on "Quality Underwriting" instructs VA field staffs to pay particular attention to previously rejected loan applications that have been submitted for reconsideration yet you oppose the MBA recommendation that you develop a system to identify a loan previously rejected by the lender using the automatic program. Aren't these inconsistent positions?

Response: We do not consider these to be inconsistent positions. Our instructions to our field staff were directed at cases in which VA reverses its own underwriting decision to reject an application. Our review of closed loans disclosed that VA underwriters will occasionally reverse their rejection decision on emotional appeals. Our instructions were intended to stop such reversals.

We do want the underwriting decision to be based on all the available facts. The fact that a lender did not consider an application approvable is one additional factor that could be of some value. Our concern with the MBA recommendation is the need to develop a "system". A system, as proposed by MBA, would require all lenders to report to VA each time they reject a veteran's application or that they were submitting a loan previously rejected by another lender. There would also be a problem in collecting reject information from lenders who do not generally participate in the VA program.

The lender's report would have to include copies of the documentation on which the decision was based; otherwise VA could not be certain that the lender's decision was soundly based. We believe that reporting of this nature would impose an additional paperwork burden on lenders and VA field offices. We also believe that it would be difficult to enforce a requirement that lenders file such reports with VA. Lenders may wish to voluntarily advise the local VA office of their decision to reject a loan. In such cases, we will consider that fact in our underwriting analysis.

Question 2. You state that you are developing a computerized capability to better identify lenders with a higher than acceptable record of defaulted loans. When will this be done?

Response: The computer system should begin operations in 1986. Lenders which are identified as having a higher than acceptable record of defaulted loans will receive additional training and counseling; will be subject to more intense reviews of their work; will be limited to prior-approval processing only; could be suspended from participation in the program if no improvement in the performance is noted. The action taken by VA in any particular case will depend on the facts of the case.

Question 3. What effect, if any, will the recent changes imposed by Fannie Mae have on the VA home loan guaranteed program?

Response: FNMA's actions should not have a profound impact on VA's home loan program for two reasons:

o Unlike FNMA, VA does not use ratios as determining factors in deciding whether or not to approve a veteran's loan. Rather, VA uses the residual income method of qualifying veteran borrowers.

o FNMA does not buy a significant percentage of new VA loans. Most VA loans end up in GNMA, not FNMA pools.

The impact VA will experience will be more of a "ripple" effect. Most VA lenders also originate FHA and conventional loans. FNMA, GNMA, VA, FHA, and private mortgage insurance companies have all become more conscious of the need to either "tighten-up" standards or at least ensure that present standards are being adhered to.

Question 4. The Non Commissioned Officers Association recommends that you be allowed to maintain your loan portfolio and concurrently be given the authority to manage it in accordance with good business decisions instead of OMB guidelines. If you were to do this, would there be any change in the status of the Loan Guaranty Revolving Fund?

Response: The Non Commissioned Officers Association appears to be recommending that VA cease the practice of regular vendee loan sales (3-5 per year). As an alternative VA would hold the assets in its portfolio and collect the monthly income these loans generate. Loan sales would then be conducted only when the credit markets were such that VA could obtain the highest prices for its assets.

Vendee loan sales at regular intervals are absolutely necessary to maintain an adequate cash balance in the Loan Guaranty Revolving Fund. In FY 1985 VA received $678 million in net loan sales. Had VA held these loans the interest income during FY 1985 would have been less than $40 million. Therefore, the Revolving Fund would have experienced a shortfall of approximately $638 million. Vendee loan sales enabled VA to replenish the Revolving Fund and avoid financial crisis.

Question 5. When did you first advise the Inspector General regarding certain invoicing practices among certain manufacturers? When did the I.G. start to investigate?

Response: Our Atlanta Regional Office first advised the I.G. of our suspicions concerning invoice padding during December 1983. To the best of our knowledge the Inspector General inquiry began after that date.

Question 6. How closely do you monitor the agencies who manage your properties? How do you advise realtors about your foreclosed properties?

Response: VA relies on private sector management brokers and sales brokers in its acquired property sales program. Management brokers provide opinions of value, estimates of repair costs, and are responsible for ensuring the security and upkeep of properties assigned to them. VA regional office staffs regularly inspect VA-owned properties. Inspection reports submitted by the management brokers are reviewed for accuracy and completeness. The quality of maintenance, including lawn care, and the adequacy of security measures are checked during property inspections made by VA staff. The quality of the management broker's supervision of repair contractors is also checked. Management brokers who do not provide good quality service to VA will have their assignments reduced, and, if improvement does not occur, they will be replaced.

Each VA regional office maintains a mailing list of real estate brokers participating in the acquired property sales program. Sales listings are mailed to the brokers regularly, and a consolidated listing of available properties is furnished by mail at least once a month.

Regional offices also advertise the availability of VA-owned properties in newspapers and other media. We are currently testing the use of electronic bulletin board systems to provide

sales brokers with the most current information on the status of listed properties. Regional office personnel conduct orientation and training sessions for new participating brokers and make presentations about the sales program to local real estate boards and firms.

Question 7. Following foreclosure action, how actively does the VA pursue collection of the debt that has resulted from foreclosure?

Response: After the VA has paid a claim on a loan guaranty default and an accounts receivable is established, it is put in the VA's benefit payment computer system. If the veteran is receiving a pension or compensation benefit from the VA, he/she is informed that action will be taken to begin offsetting benefits to liquidate the indebtedness. If the veteran is not drawing a benefit, the account is transferred to the VA's Centralized Accounts Receivable System (CARS) where a series of collection letters are generated at 30 day intervals. If the collection letters do not result in payment in full or the establishment of an acceptable repayment plan, the account is referred to either the VA's District Counsels or the Department of Justice for litigation, depending on dollar amount. (District Counsel--$200-$1,200, Department of Justice--over $1,200.)

Question 8. Do you have any plans to do anything about the thousands and thousands of veterans who have never defaulted but who may have been overcharged for their homes. No one seems to be representing this veteran but the Vietnam Veterans of America, and that is limited to those who served in Vietnam. What happens to our WWII and Korean Conflict veterans?

Response: In a manufactured home loan, the purpose of the manufacturer's invoice, in VA's case, is to establish the maximum loan amount. VA has no authority to regulate the sales price of manufactured homes. However, in connection with the investigation, we are currently compiling a list of VA-guaranteed manufactured home loans identified by veteran's name and manufacturer of the unit securing the loan. Veterans who purchased a unit from a VA-suspended manufacturer will be informed by us that the manufacturer has been suspended, the reasons for the suspension, and the fact that they may have a possible claim against the manufacturer. Our response will not be limited to Vietnam veterans but will include all veterans that purchased a unit from a suspended manufacturer since 1979. The starting date is 1979, since the VA Inspector General is not pursuing cases before 1979.

Question 9. Have you seen a copy of the TRUTH-IN-INVOICE practices approved by MHI board directors and awaiting a Department of Justice antitrust division business letter review? Do you believe this will help you to make an informed decision about a manufactured home loan as is stated by MHI?

Response: We have just recently been provided with a copy of the MHI's TRUTH-IN-INVOICING statement. We intend to give it, and all other certification and disclosure suggestions, careful consideration. One item that should be mentioned is that MHI has no enforcement capability over manufacturers and their use of the proposed certification. Discussions are ongoing between VA staff and representatives of the manufactured home industry.

Question 10. To your knowledge, is the Manufactured Housing Industry charging veterans more than non-veterans?

Response: We are not aware of veterans being charged more than non-veterans by the Manufactured Housing Industry.

Question 11. One of our witnesses today recommends a change in VA procedures so that you provide appraisals on manufactured homes rather than rely on the certification process. Would you give me your opinion?

Response: During the initial stages of the Inspector General's investigation into suspected fraud in the manufactured home industry it was agreed, at the request of the Inspector General, that no changes in procedures would be made. It appears that investigation is in the final stages and the Inspector General has withdrawn his request for no changes to our procedures. Input from all interested parties, including the Department of Housing and Urban Development and the manufactured home industry will be sought and given careful consideration. One item being studied is the use of appraisals for determining the maximum loan amount for loans secured by manufactured homes.

Question 12. How will the elimination of HUD's minimum property standards affect the VA Home Loan Guaranty Program?

Response: HUD's revision to its present procedures will, for the most part, allow the use of local building codes in lieu of the MPS. The VA will act in a similar fashion by allowing the use of local building codes as construction criteria. The responsibility for ascertaining compliance with the applicable code(s) will lie with the local authority having jurisdiction. VA fee compliance inspectors will continue to be responsible for reporting conformity with the plans and specifications which formed the basis for VA's value determination and report observed workmanship and materials or conditions which are not conducive to a safe, sound and sanitary structure. We believe that the quality of housing stock will not be jeopardized and the security for loans which VA guarantees will be protected.

In rural areas where no state or local code is in use we propose to apply the Council of American Building Officials (CABO) One and Two Family Dwelling Code. We feel that the use of the CABO Code will provide an acceptable level of protection where there are no local codes in force.

Questions from Congressman Christopher H. Smith

Question 1. What happens in the VA to assure that an adequate number of fee basis appraisals are reviewed by VA staff?

Response: Every appraisal completed by a fee basis appraiser is reviewed by a VA staff employee prior to issuance of the Certification of Reasonable Value with the exception of those instances in which a regional office utilizes the services of qualified and trained fee contract personnel to review appraisals during a period of heavy workload. In addition, based upon an average of the sum of the appraisal reports received during the previous 3 month period, our regional offices are required each month to review at least 10 percent of the appraisal reports completed by fee basis appraisers on their fee roster.

Question 2. How does the VA police or supervise its fee basis appraisers?

Response: As we have indicated, every appraisal is reviewed by a VA staff employee and at least 10% are required to be field reviewed each month (based upon a 3 month average). These reviews are made to determine if the appraisal has been prepared in accordance with acceptable appraisal techniques and instructions issued by the VA regional offices. Performance files are maintained in the regional offices for each appraiser on the fee roster. These files contain records of errors, delays in production, field reviews, letters of admonishment and other material pertaining to the performance of fee appraisers. Internal control procedures have been implemented which require that fee appraisers be properly admonished for unsatisfactory performance. These internal control procedures further require that regional office management review operations on an ongoing basis to ensure that employees under their control are applying these established controls.

Question 3. Recognizing that you may not be able to comment in full, could you tell us what is happening with respect to the appraisal investigation in Camden, New Jersey?

Response: We defer to the Inspector General on this matter.

Question 4. What happens to a manufactured home when foreclosure takes place?

Response: When a manufactured home is repossessed, the loan holder is required to notify VA. VA obtains an appraisal of the unit and determines its current reasonable value. This figure is furnished to the holder as the minimum resale price. After it resells the home, the holder submits its claim under loan guaranty to VA. In computing the claim payable, VA will credit the veteran's debt with the actual proceeds of sale or the minimum resale price, whichever is greater.

Question 5. The investigations with respect to manufactured homes has centered on those situations where foreclosures have taken place. What is VA doing with respect to those situations where the price of manufactured homes has been inflated, thus causing the veteran to pay a higher price for the home, and thus causing the VA to guarantee it with the resultant possibility of a greater loss through foreclosure?

Response: It must be understood that the purpose of the manufacturer's invoice, in VA's case, is to establish the maximum loan amount. VA has no authority to regulate the sales price of manufactured homes. However, in connection with the investigation, we are currently compiling a list of VA-guaranteed manufactured home loans identified by veteran's name and manufacturer of the unit securing the loan. Veterans who purchased a unit from a VA-suspended manufacturer will be informed by us that the manufacturer has been suspended, the reasons for the suspension, and the fact that they may have a possible claim against the manufacturer. Negotiated settlement agreements that have been reached with suspended manufacturers included payments to the VA in compensation for VA's actual and future losses suffered by the VA as a result of the manufacturers' actions.

Question 6. Are you able to tell us of any disciplinary action of fee basis appraisers or staff employees with respect to the Camden situation?

Response: A broker/appraiser who is currently incarcerated as a result of his involvement in this fraudulent activity, has been placed on a notice of intent to suspend by HUD; this action is the basis for a reciprocal suspension by VA, and VA is also looking into the possibility of taking independent debarment action. An employee of a lender who was one of the principal participants in the situation has been debarred by the VA. An ongoing investigation into VA staff involvement has not at this time implicated any VA employees.

1125 Fifteenth Street, N.W.
Washington, D.C. 20005

Mortgage Bankers Association of America

Robert J. Spiller
President
(202) 861-6500

July 3, 1985

Mr. Harry N. Walters
Administrator of Veterans Affairs
Veterans Administration
810 Vermont Avenue, NW
Washington, DC 20420

Dear Mr. Walters:

Enclosed is a final report of the Mortgage Bankers Association of America's VA Task Force. I appointed this Task Force in February 1985 to study the VA Home Loan Guaranty Program and to recommend Program changes that will reduce losses to VA and to mortgage lenders, without disadvantaging credit worthy veterans.

I believe a reexamination of the VA Home Loan Guaranty program is vital for four reasons. First, disinflation of home prices has occurred in some geographical areas, thus producing sharp differences in the value of homes when loans are made, and if problems arise with the loan later on. Second, the incidence of VA "no-bids", in which the VA pays the guaranty and leaves the lender with the foreclosed property, has increased, creating significant monetary losses for VA lenders. Third, the Program has come under close scrutiny by Congress and the Administration because the Program operates at a significant deficit at a time when fiscal pressures on all government agencies are especially acute. Finally, the Administration is attempting to increase sharply the VA Funding Fee in part at least based on the justification that additional revenues are necessary to eliminate the Loan Guaranty Fund deficit.

In an effort to reduce VA foreclosure losses to both VA and the mortgage lending industry and to reduce the incidence of VA "no-bids", the Task Force met twice with Robert O'Toole and other VA staff. Thorough discussions were held concerning origination and underwriting procedures, as well as, foreclosure and servicing issues. The Task Force did not produce one single recommendation to reduce losses on existing VA guaranteed loans. Instead, the Task Force concluded that there are numerous changes the VA and VA Lenders may adopt to reduce future losses.

Some of the recommendations of the Task Force can be implemented immediately by mortgage lenders. Other recommendations will require action by the VA and, in some instances, Congressional action may be needed.

In this era of fiscal responsibility, I am urging our members to adopt recommended changes that will enable the VA Program to thrive and continue to enable all qualified, creditworthy veterans to achieve homeownership. To further this goal, I urge VA to consider our recommendations.

Sincerely,

Robert J. Spiller

Robert J. Spiller
President

I. Origination/Underwriting

RECOMMENDATION: VA should reevaluate its Home Loan Guaranty Program underwriting standards with an eye toward revising those standards to assure that only credit worthy veterans are found qualified for VA loans.

VA has always strived to ensure that only financially capable, credit-worthy veterans receive VA home loans. However, because of the benefit nature of this program, it is VA's policy to resolve doubts in favor of the veteran when, in good conscience and with propriety, it is possible to make a favorable determination. VA is continually studying loans that end in foreclosure in an attempt to identify characteristics common to these loans and to determine what actions should be taken to reduce the probability of default.

Realizing the effects of continued high levels of defaults and foreclosures coupled with disinflation of home prices, VA published DVB Circular 26-85-22, Quality Underwriting, on May 30, 1985. In this issue, VA identifies specific areas in the credit underwriting procedures that needed improvements.

As part of this recommendation, it is suggested that VA consider the use of ratios in its credit underwriting. VA's use of the residual method of underwriting in lieu of prescribed ratios has proven successful overall for our unique type of housing program. To accurately assess the two methods of underwriting by simply looking at the default and foreclosure rates would be difficult at best since the conventional market and FHA do not make 100 percent loans. VA has no plans to convert to the ratio method of underwriting at this time.

RECOMMENDATION: VA Lenders should consider stiffening their individual company's underwriting guidelines for VA loans beyond those imposed by VA.

VA has never tried to impose its underwriting guidelines on the private sector. Our credit standards are provided to VA lenders for information purposes and to assist them in processing VA home loans. VA would not therefore be opposed to lenders stiffening their underwriting guidelines for VA loans. This may help to eliminate some loan applications that are submitted to VA that are clearly rejects.

VA has already begun a reexamination of its approval standards. This is evidenced by the recent publication of DVB Circular 26-85-18, Balance Available for Family Support Guidelines and DVB Circular 26-85-22, Quality Underwriting. A copy of each circular is provided. Also, seminars will be held in September, 1985 in Denver and Philadelphia. Loan Guaranty Officers from each regional office will attend these seminars and the agenda will include discussions on credit underwriting. In addition, the VA's Office of Inspector General is conducting a study of VA home loans which the Department of Veterans Benefits fully supports. Valid recommendations will be implemented.

RECOMMENDATION: VA loan field offices should be instructed that loan underwriting decisions should be made exclusive of "pressure" imposed on that office by veteran applicants and/or real estate sales agents.

VA's staff underwriters are trained, as are underwriters for FHA and conventional lenders, to only approve those applicants that are truly creditworthy. However, as is evidenced by the amount of foreclosures of VA, FHA and conventional loans, this is not always possible. Even the most creditworthy individual can encounter unforeseen problems that may result in the eventual loss of a home. If a favorable determination can be made in the case of a marginal VA application, in good conscience and with propriety, the loan may be approved. VA's circular "Quality Underwriting" instructs VA field staffs to pay particular attention to previously rejected loan applications that have been submitted for reconsideration. For example, only when new and compelling information is submitted for reconsideration should a case be reopened and approval of the loan be considered. Emotion or "pressure" should not be the basis for approving a loan that was previously rejected based on application of VA's credit standards. The circular also addresses other specific underwriting areas that may require careful scrutiny before a final decision is made. Continual reviews of foreclosed loan files and post-audit files provide insight into underwriting deficiencies which can then be corrected.

In this recommendation, it is also suggested that the veteran applicant be restricted from having direct access to VA field offices.

VA administers its home loan program on behalf of the nation's veterans. Therefore, VA believes that veterans should have direct access to field stations for assistance and guidance in benefit matters.

RECOMMENDATION: VA should encourage VA lenders to increase the use of the VA Automatic Program.

In the past eight years, the percent of VA loans closed on the automatic basis has increased more than fivefold from 8.33 percent in 1976 to 43.52 percent in 1984. To make the automatic program more accessible to nonsupervised lenders, in 1982 VA relaxed its qualification standards which has enabled many newly established institutions to participate as VA automatic lenders. VA will continue to encourage lenders to make use of its automatic program.

VA does not believe it would be in our best interest to furnish lists of approved automatic lenders to builders and real estate agents. This practice could well be construed by those lenders not having the automatic authority as favoritism on the part of VA. Lenders approved for automatic processing are well aware that this authority is a valuable marketing tool and therefore, they are already using the automatic authority to promote new business.

This recommendation also points out that the delinquency and foreclosure rates under the VA Automatic Program are consistently less than these rates under the VA prior approval program. This is true because loans approved on the automatic basis represent the best credit risks and are those veterans who meet all of the VA's credit standards without difficulty.

Automatic lenders are aware that if they develop a record of closing loans which do not meet VA's credit standards, their automatic authority may be terminated. Most lenders want to minimize the risk of losing their very valuable automatic authority and only close "premium" loans on the automatic basis. Because they fall into a higher risk category, it is to be expected that loans approved under the prior approval basis would suffer a higher rate of default than those processed under the automatic procedure.

RECOMMENDATION: VA should develop a system that identifies a loan that is resubmitted to VA on a prior approval basis or resubmitted to another VA Automatic Lender when it was rejected by a lender using the Automatic Program.

All lenders have their own credit underwriting standards and different levels of risk. Because one lender may not find it possible to approve a veteran's loan

application does not mean that a different lender may find that the loan can be approved. A veteran could be unjustly denied a home loan because of unnecessary bias on the part of a VA staff underwriter or a lender's underwriter who had prior knowledge that the veteran's loan application had previously been rejected.

A lender may learn of recent inquiries made by creditors on a particular loan applicant by means of data available in credit bureau records in many cases. If a loan applicant is found to have made previous applications for mortgage financing the lender may wish to pursue the issue further. In any event, the same procedures used by lenders to identify potential borrowers who have been rejected by other lenders can be applied to the VA program.

Concerning the "pressure" placed upon a lender to submit a loan under the prior approval procedure that had been rejected under the automatic procedure, the VA feels that lenders are able to respond to these pressures without unnecessary government intrusion in the mortgage origination process.

RECOMMENDATION: VA Lenders should determine if their companies are sending rejected VA automatic loans through VA on a prior approval basis.

The VA agrees that the internal control procedures of lenders should be adequate to preclude submitting previously rejected applications to the VA on a prior approval basis if the lender so desires. However, since credit underwriting is not an exact science, there may be instances when an underwriter may feel uncomfortable with a loan application being processed on the automatic basis and may desire to submit the loan to VA as a prior approval submission. Such applications rejected when processed on the automatic basis should be carefully reviewed and the reasons for the disapproval given to the applicants. (Lenders may also wish to advise the appropriate VA office of their decision.)

II. Appraisals

RECOMMENDATION: Lenders' underwriters should develop expertise in appraisal underwriting.

VA agrees that lenders should review the appraisal reports. To assist in that endeavor, on April 12, 1985, field stations were instructed to send to the requester of an appraisal of individual existing or proposed construction a copy of the appraisal report with the related Certificate of Reasonable Value.

It is VA policy that the Certificate of Reasonable Value as it relates to value or any other aspect may be reconsidered upon the request of a party of interest; i.e., the requester, the buyer, the seller, the lender or broker. Should lenders wish to question a Certificate of Reasonable Value an additional appraisal does not have to be ordered. The outstanding case can be reconsidered. The instructions to our field stations state that the valuation stipulated on a Certificate of Reasonable Value is conclusive as to the VA. However, the instructions also provide that a valuation may be reduced, withdrawn, or modified under certain conditions and if such action is necessary to render the valuation to be consistent with the market.

RECOMMENDATION: A standard appraisal form should be developed for use by VA, FHA, FNMA, and FHLMC.

The VA has been working with HUD, FNMA, FHLMC, and the Society of Real Estate Appraisers to develop an appraisal report form which can be used by all of the above entities. VA is pleased to report that a test of what is believed to be a workable report form is planned for an October beginning. VA and HUD are preparing instructions to the field stations which will participate in the test.

RECOMMENDATION: VA should require photographs of comparables on appraisals.

There is some merit to the suggestion that reviewers of appraisal reports can benefit from having photographs of the market comparables used by the appraiser. However, there are matters to be considered with regard to obtaining pictures; e.g., appraiser (or photographer) confrontations with the property owner (or occupant) and trespassing. This recommendation is still under consideration.

RECOMMENDATION: VA should develop a system whereby at the time of foreclosure the name of the appraiser should be identified in order to determine if that appraiser's loans that end in foreclosure consistently have significantly lower values at the time of foreclosure than at the time of origination.

In the process of review of liquidation appraisal reports the appraisal review staff is required to compare the origination appraisal with the current appraisal. If, in the review process, an origination appraisal is determined to have been improper for any reason the appraiser would be notified and a copy of the notification filed in the appraiser's performance folder. These folders are reviewed at least annually and disciplinary action, which may range from counseling to suspension, is taken in cases of appraisers who demonstrate unsatisfactory performance. VA is of the opinion that there is an effective system for monitoring appraisers performance in place at this time.

RECOMMENDATION: VA should consider allowing lenders to select appraisers.

Delegating the selection of fee appraisers to lenders, VA believes would not be in the best interests of veterans or the Government. Similar proposals have been made in the past and based on in-depth studies, VA has felt compelled to reject such proposals. The Loan Guaranty Program would become more susceptible to fraud and abuse. The integrity of the property appraisal is critical to the success of the Loan Guaranty Program. If lenders were given authority to select appraisers there would be a strong tendency to chose those who would accommodate the needs of the lenders. Carried one step further, this could translate into higher realty values which mean higher loan amounts, therefore, unscrupulous lenders and appraisers could take advantage of veterans and the VA. For the preceding reasons, VA is not in favor of adopting this recommendation.

III. SERVICING AND FORECLOSURE

RECOMMENDATION: VA should exclude from indebtedness the amount of interest that accrues during periods of forebearance. This should include bankruptcy workouts.

This recommendation has been implemented. DVB Circular 26-85-28 (copy attached), issued on July 5, 1985, resulted from earlier discussions between VA and MBA.

It established procedures under which VA may predetermine the net value of a property securing a GI loan and commit to accepting conveyance of the property for the net value in the event foreclosure is ultimately necessary after a period of forbearance. In return, the lender would agree to exclude interest which accrued during the period of forbearance when filing its claim under loan guaranty. This Circular does not specifically address bankruptcy work-outs; however, its provisions could also be applied to a situation in which the borrower has filed for bankruptcy under Chapter 13 and is meeting his or her obligation under the terms of the plan.

RECOMMENDATION: VA should encourage lenders to contract with third-party counselors for the purpose of making pay-out arrangements with delinquent borrowers.

The primary responsibility for servicing a delinquent loan rests with the lender. VA has no objection to lenders contracting with third-party counselors for assistance in that area; however, the cost of such counseling services should not be passed on to the veteran-borrower.

RECOMMENDATION: VA lenders should review VA foreclosed loans to determine the major areas creating losses so that VA can use this information in redesigning its underwriting criteria.

We would be pleased to review any data developed by lenders which would point out weaknesses in VA's loan underwriting standards.

RECOMMENDATION: VA lenders need to be aware that in the event of foreclosure, if the house is abandoned and vacant, lenders can proceed with foreclosure without approval from the VA field office

Lenders are expected to terminate loans as quickly as possible when there is no alternative to foreclosure. Abandonment of a property constitutes just such a situation, and we would appreciate the cooperation of the MBA in reminding lenders they may take prompt action under these circumstances. VA must, however, be informed of the action being taken.

RECOMMENDATION: VA lenders should make use of the procedure allowing VA to pay a partial claim in those instances where someone can take over the property for less than is due.

We understand this procedure is being used by private mortgage insurers and encourage its application to GI loans. VA will consider payment of a partial claim in situations where the veteran sells his or her property to either an assumer or to a cash purchaser.

RECOMMENDATION: VA lenders should make use of the procedure that allows veterans to be paid for a deed in lieu of foreclosure as long as VA approves the deed in lieu.

VA has no objection to a lender paying a consideration for a deed in lieu of foreclosure under these circumstances.

RECOMMENDATION: VA field offices should issue bidding instructions on foreclosed properties on a timely basis.

We share the MBA's concern over unnecessary costs incurred as a result of the postponement of foreclosure sales. Many of our offices have initiated procedures which allow lenders to order liquidation appraisals by telephone in order to reduce the number of sales which are delayed because a current appraisal has not been completed. Further, when lenders have informed us of recurring problems with sale postponements by particular VA offices, we have advised the offices of our concern and kept a follow-up until improvements were reported. We are currently preparing a release to all VA offices which will stress the importance of issuing timely advice to lenders in order to minimize the number of sales which must be postponed.

RECOMMENDATION: VA should combine the "Notice of Default" and "Notice of Intention to Foreclose" into a new, single notification to the VA and allow this single form to be filed after the 60th day of default.

With regard to a consolidated Notice of Default and Notice of Intention to Foreclose, we believe it is important to retain separate forms because each notice concerns a distinctly different action. The Notice of Default may be filed after the 60th day of default and must be filed within 45 days thereafter, if no payments

are received during the interim. Many defaults are, however, reported while a repayment schedule or forbearance agreement is in effect. In other cases, work-out arrangements are made after the notice has been filed. Since most defaults reported to VA eventually result in repayment of the delinquency and reinstatement of the account, concurrent filing of the Notice of Intention to Foreclose should be reserved for situations in which the lender's servicing has clearly shown there is no feasible alternative to foreclosure.

VA currently requires lenders to refrain from filing a Notice of Intention to Foreclose until a default has continued for at least 90 days. An exception may be made when the property is abandoned or subject to extraordinary waste or hazard. In the normal course of servicing a defaulted loan, however, 90 days is a minimal amount of time for contacting the veteran, reviewing his or her situation, and making an informed decision as to the prospects for reinstatement. In light of the number of defaults which are now being cured after a Notice of Intention to Foreclose has been filed, and considering the fact that referral of a loan to an attorney to initiate foreclosure increases costs and may make reinstatement more difficult, we believe VA's current requirements adequately balance the interests of the lender, the veteran and the Government.

Department of Veterans Benefits
Veterans Administration
Washington, D.C. 20420

DVB Circular 26-85-22

May 30, 1985

QUALITY UNDERWRITING

1. VA is continually attempting to improve the quality of the loans it guarantees, while still ensuring that each qualified veteran has a fair opportunity to own a decent home.

2. It serves no valid purpose to approve a loan for a veteran who will be unable to meet the repayment terms or is not a satisfactory credit risk since it could well result in the veteran losing the home, a debt being owed by the veteran to the U.S. Government, and an adverse effect on the veteran's credit standing. Investors and servicers also have a strong financial interest in determining that sound credit underwriting practices are employed in approving loans to ensure that the veteran has the ability and willingness to repay the loan.

3. Although the economy continues to improve, defaults and foreclosures remain at relatively high levels. VA paid over 23,000 claims in Fiscal Year 1984, an increase of 16 percent over Fiscal Year 1983. Most of these defaults cannot be attributed to poor or liberal underwriting. However, there can be no dispute that some VA loans that end in default should not have been made. Because of the high loan-to-value aspect of our program, it is critically important that each underwriter use sound judgment. A few years ago, the inflationary environment caused property values (and equity) to go up so quickly that underwriting errors and bad decisions had little effect on default rates. However, with decreased inflation and property values remaining relatively stable, there is simply no room for errors or lax decisionmaking.

4. Recent reviews of defaulted loans, especially loans that went into default within the first year or two, reveal numerous areas in which improvements may be made in the underwriting process. Examples are:

a. Reporting the borrower to be a salaried employee, when in fact, he/she works on commission, is a contract employee, or is actually self-employed.

b. Allowing income information to be handcarried by the borrower, sales agent, or party other than the lender.

c. Addressing verification forms to an individual chosen by the borrower, rather than to "Personnel" or "Payroll" or "Accounts Receivable" etc.

d. Failing to compare the documented information with the borrower's initial application, (e.g. ignoring debts, judgments, bankruptcies, or alimony and child support obligations just because they don't show up on the credit report).

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We encourage all participants to take an active interest in improving the quality of VA loans. More training, implementation of quality control systems, and adherence to established underwriting standards are just several ways to ensure that loans are made only to qualified borrowers.

6. Lenders have a responsibility to fully develop each case, prior to its submission to VA. Each case submitted by the lender on either the prior-approval or the automatic basis includes a certification by the lender that the loan meets the income and credit requirements of the law. If it is found that a lender has a record of submitting loans which are poorly developed, incomplete, fraudulent, or which clearly do not qualify for guaranty, consideration will be given to suspending that lender from participation in VA's program, withdrawal of its automatic authority, or other actions as appropriate. VA may also suspend individual employees who are found to have committed fraud or were responsible for material misrepresentation in the soliciting, processing, or approval of VA loans.

7. A recent study of the default rates of prior-approval versus automatic loans for Fiscal Years 1970 through 1984 revealed that a prior-approval loan is more than twice as likely to end in foreclosure than a loan processed on the automatic basis (4.92% for prior approval versus 2.12% for automatic). While we are well aware of several understandable explanations for this difference (e.g. automatic loans usually involve Grade "A" borrowers while prior-approval loans require a much more difficult underwriting decision), these percentages point out areas for additional attention on the part of VA underwriters such as:

a. Are too many cases in which the original decision was to reject the loan reopened and approved without new and compelling information?

b. Are too many poorly developed cases approved when, if properly developed, they would be rejected?

c. Are VA underwriters too anxious to resolve doubt in the veteran's favor even though there is no reasonable basis for such a resolution?

d. Are enough "marginal" prior-approval applications being reviewed by more than one VA underwriter in order to get a consensus on what the proper action should be?

e. Are automatic lenders using the prior-approval procedure even after their own underwriter has already decided that the loan is not an acceptable risk?

8. Stations should ensure that all of its Loan Specialists are furnished with a copy of this circular and are familiar with the areas in which improvements can be made in the underwriting of prior-approval loans. When possible, stations should use training sessions to discuss this circular as well as specific cases.

Department of Veterans Benefits
Veterans Administration
Washington, D.C. 20420

DVB Circular 26-85-18

May 3, 1985

BALANCE AVAILABLE FOR FAMILY SUPPORT GUIDELINES

1. The purpose of this circular is to announce a change in VA policy allowing stations to provide lenders and others outside the VA, with locally developed guidelines for determining the "balance available for family support." Previously, those stations who developed such guidelines, used them for internal training purposes only. Recently, many lenders have been inquiring about the availability of such guidelines in order that they may be more consistent with VA policy in underwriting VA guaranteed loans.

2. The credit underwriting policy and procedures established by VA for use by its field stations are contained in DVB Circular 26-80-11, Credit Standards. These credit standards are furnished to lenders for their information and guidance. To aid in reviewing loan applications, VA Form 26-6393, Loan Analysis, the format of which has been adopted by many lenders for use in analyzing proposed loans, is used by the VA. Item 44 of the form, Balance Available for Family Support, is the figure that should be compared to the information in the balance available for family support guidelines.

3. Although the balance of income available for family support is a significant factor to be considered in reviewing a veteran's loan application, it should never be the sole criterion for approving or rejecting a loan. Among other important factors to be considered are:

a. The borrower's demonstrated ability to accumulate liquid assets (e.g., cash, bonds).

b. The borrower's demonstrated ability to use credit wisely and to refrain from incurring an excessive number of debts.

c. The relationship between the proposed shelter expense and the amount the borrower is accustomed to paying.

d. The number and ages of borrower's dependents.

e. The locality and economic level of the neighborhood where the property is located.

f. The likelihood of increases or decreases in borrower's income.

g. The borrower's work experience and history.

h. The borrower's demonstrated willingness and ability to meet voluntarily incurred obligations in the agreed-upon manner (e.g., making payments on time).

i. The amount of any downpayment made.

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DVB Circular 26-85- 28 July 5, 1985

6. Predetermination cases will require extraordinary monitoring by both VA and the holder to ensure that the forbearance extended is and remains appropriate, and that foreclosure is not delayed in the event the borrower does not resume payments in accordance with the forbearanc agreement. Any cutoff date established under this procedure may be adjusted if the borrower makes some payments but is ultimately unable to reinstate the account.

7. Copies of this circular will be reproduced and distributed locally for holders and servicers. Copies of such releases need not be submitted to Central Office.

8. DVB Manual M26-4 will be adjusted accordingly.

R. J. VOGEL
Chief Benefits Director

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Department of Veterans Benefits
Veterans Administration
Washington, D.C. 20420

DVB Circular 26-85-28

July 5, 1985

FORBEARANCE ON GI LOANS IN DEFAULT AND
PREDETERMINATION OF NET VALUE

1. When a GI loan is in default, and servicing indicates there is a reasonable prospect that the borrower will be able to resume payments and reinstate the account in the foreseeable future, loan holders have traditionally cooperated with VA in extending forbearance to the homeowner. In so doing, holders ran little risk of loss since, if foreclosure were ultimately necessary, VA would likely offer to purchase the property under 38 CFR 36.4320 and reimburse the holder for the balance of the indebtedness.

2. However, implementation of Public Law 98-369, The Deficit Reduction Act of 1984, has increased the number of cases in which VA does not offer to purchase the property under 38 CFR 36.4320. Under these circumstances, holders have pointed out that a decline in the net value of the property and/or an increase in the loan indebtedness occurring during a period of forbearance could well make the difference between VA specifying or not specifying an amount in connection with a foreclosure. In some cases, holders would be reluctant to extend forbearance as a result of their concern that such action would not be prudent from a business standpoint.

3. In cases in which foreclosure is imminent and (1) a holder indicates it will extend additional forbearance for a fixed period of time provided VA furnishes some assurance that an amount will be specified if foreclosure is ultimately necessary, and (2) the holder volunteers to accept a cutoff date which will limit the amount of the total indebtedness for purposes of the final accounting, it may be in the best interests of the Government and the veteran-borrower for VA to agree to the holder's proposal.

4. In such cases VA will obtain a current appraisal of the property and determine its net value to the Government. The net value will be compared with the projected debt at foreclosure if no forbearance were extended. VA may then advise the holder of the net value and that such value will remain in effect for a fixed period of time. The period allowed should not exceed the amount of time the holder intends to extend forbearance plus reasonable additional time to allow for resolution of the default through reinstatement or completion of foreclosure. If the predetermination is intended to last for an extended period, the appraisal will be updated after 6 months in order to ensure that continuation will not expose VA to undue risk.

5. Such a predetermination will only be made if VA and the holder have agreed to fix a cutoff date which will govern for purposes of computation of the indebtedness. The cutoff date will normally be the date a foreclosure sale would have taken place if no forbearance were extended. This procedure would not be applicable if the net value of the property is less than the unguaranteed portion of the debt, or if there were no reasonable basis for the extension of forbearance.

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